

OFFICIAL TRANSCRIPT OF PROCEEDINGS BEFORE THE POSTAL REGULATORY COMMISSION

In the Matter of:)	
)	
RATE ADJUSTMENT DUE TO)	Docket No. R2010-4
EXTRAORDINARY OR)	
EXCEPTIONAL CIRCUMSTANCES)	

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POSTAL REGULATORY COMMISSION

In the Matter of:)
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RATE ADJUSTMENT DUE TO) Docket No. R2010-4
EXTRAORDINARY OR)
EXCEPTIONAL CIRCUMSTANCES)

Hearing Room
Postal Regulatory Commission
901 New York Avenue, N.W.
Washington, D.C.

Volume 3
Thursday, August 12, 2010

The above-entitled matter came on for hearing pursuant to notice, at 9:32 a.m.

BEFORE:

HON. RUTH Y. GOLDWAY, CHAIRMAN
HON. TONY HAMMOND, VICE-CHAIRMAN
HON. DAN G. BLAIR, COMMISSIONER
HON. Nanci E. LANGLEY, COMMISSIONER
HON. MARK ACTON, COMMISSIONER

APPEARANCES:

On behalf of the United States Postal Service:

ERIC KOETTING, Esquire
DAVID H. RUBIN, Esquire
United States Postal Service
475 L'Enfant Plaza, S.W.
Washington, D.C. 20260

Heritage Reporting Corporation
(202) 628-4888

APPEARANCES: (cont'd.)

On behalf of the Office of the Consumer Advocate:

JIM WACLAWSKI, Esquire
PAM THOMPSON, Esquire
NATALIE REA, Esquire
Postal Regulatory Commission
Office of Consumer Advocate
901 New York Avenue, N.W.
Washington, D.C.
(202) 789-6833

On behalf of Greeting Card Association:

(No Appearance.)

On behalf of National Association of Postmasters of the United States:

(No Appearance.)

On behalf of National Association of Letter Carriers:

(No Appearance.)

On behalf of David B. Popkin:

(No Appearance.)

On Behalf of National Rural Letter Carriers Association:

(No Appearance.)

C O N T E N T S

WITNESSES APPEARING:

Frank Neri

James M. Kiefer

<u>WITNESSES:</u>	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RECROSS</u>	<u>VOIR DIRE</u>	<u>COMMISSION</u>
Frank Neri	--	--	--	--	--	303
James M. Kiefer	361	--	--	--	--	---

<u>DOCUMENTS TRANSCRIBED INTO THE RECORD</u>	<u>PAGE</u>
Institutional responses to questions posed at July 2010 technical conferences	258
Institutional responses to Presiding Officer Information Requests	294

E X H I B I T S

<u>EXHIBITS AND/OR TESTIMONY</u>	<u>IDENTIFIED</u>	<u>RECEIVED</u>
Institutional responses to questions posed at July 2010 technical conferences	256	257
Institutional responses to Presiding Officer Information Requests	256	257
Statement of James M. Kiefer on behalf of the United States Postal Service, 7-6-10	362	362
Responses of James M. Kiefer to Presiding Officer Information Requests	362	362

P R O C E E D I N G S

(9:32 a.m.)

CHAIRMAN GOLDWAY: Good morning, ladies and gentlemen. The hearing will come to order. This is our third and, in the absence of any unexpected developments, final day of hearings in Docket No. R2010-4.

For the record, I am Ruth Goldway, Chairman of the Postal Regulatory Commission and presiding officer in this proceeding. Joining me today on the dais are Vice Chairman Hammond and Commissioners Acton and Langley. Commissioner Blair has been delayed, unfortunately, as a result of the weather, but we're expecting him shortly.

Today's hearing is being web broadcast. Once again, we request those in attendance to please turn off your cell phones, BlackBerrys or other personal communication devices in order to avoid interference with the overhead microphones and audio system here in the hearing room. Thank you for your consideration and cooperation.

Today we will hear from Frank Neri, Manager of Processing Operations in the Headquarters Network Operations Group, and James M. Kiefer, a pricing economist for the Postal Service. Only the Commission

1 will ask questions of these postal representatives.

2 Nevertheless, interested parties have been
3 given the opportunity to suggest questions to the
4 Commission, and a number of groups and entities have
5 filed suggested questions. The Commission appreciates
6 the effort that has gone into the preparation of these
7 questions.

8 As previously discussed, some of these
9 questions will be asked today while others may appear
10 in additional Presiding Officer Information Requests
11 that include some of the suggested questions, as well
12 as followup questions from these hearings.

13 At this point I would like to give my
14 colleagues an opportunity to make any opening remarks
15 they would wish. Vice Chairman Hammond?

16 VICE CHAIRMAN HAMMOND: No thank you, Madam
17 Chairman.

18 CHAIRMAN GOLDWAY: Commissioner Acton?

19 COMMISSIONER ACTON: Thank you, Madam
20 Chairman. I just want to thank the witnesses for
21 their time and testimony.

22 CHAIRMAN GOLDWAY: And Commissioner Langley?

23 COMMISSIONER LANGLEY: I have no response
24 right now. Thanks.

25 CHAIRMAN GOLDWAY: Okay. Does any

1 participant have a procedural matter to discuss before
2 we begin?

3 (No response.)

4 CHAIRMAN GOLDWAY: If not, our first order
5 of business is introducing into the record certain
6 information previously provided by the Postal Service.

7 That information was provided in the form of
8 written responses to several questions raised during
9 our July 2010 technical conferences and written
10 responses to Presiding Officer Information Requests
11 that were answered by the Postal Service as an
12 institution.

13 (The documents referred to
14 were marked for
15 identification.)

16 CHAIRMAN GOLDWAY: Mr. Koetting, have you
17 had a chance to review the packets containing these
18 Postal Service responses to determine if they remain
19 accurate?

20 MR. KOETTING: They were, Madam Chairman.
21 We did take the opportunity to correct one typo. I
22 neglected to add the final E in the word service in
23 the header of one question. We penciled that in.

24 CHAIRMAN GOLDWAY: Thank you. Will you
25 please provide the reporter with two copies of the

1 corrected packet? Those responses are received into
2 evidence and are to be transcribed.

3 (The documents referred to,
4 previously identified, were --
5 received in evidence.)

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DOCKET NO. R2010-4
INSTITUTIONAL RESPONSES TO
QUESTIONS POSED AT THE TECHNICAL CONFERENCE

July 19, 2010 Technical Conference

- Responses of the United States Postal Service to Informal Questions Regarding Forecasting Matters Posed At the Technical Conference, filed July 26, 2010
- Response of the United States Postal Service to Informal Question Regarding Cost Reduction Programs Posed at the Technical Conference on July 19, 2010, filed July 27, 2010

July 27, 2010 Technical Conference

- Response of the United States Postal Service to Informal Question Regarding Cost Reduction Programs Posed at the Technical Conference on July 27, 2010, filed August 2, 2010
- Response of the United States Postal Service to Informal Question Regarding Flats Strategy Programs Posed at the Technical Conference on July 27, 2010, filed August 3, 2010

**Response of United States Postal Service to Request for Additional
Information
Related to Volume Forecasting from Technical Conference on July 19, 2010**

1. Volume-Adjustment Multipliers

At the July 19, 2010, Technical Conference, the Postal Service was asked to document the volume-adjustment multipliers found at row 83 of sheet 'Comp. Mult' of the volume forecasting spreadsheets filed in USPS-R2010-4/8.

As explained at the conference, the purpose of the volume-adjustment multipliers is to adjust base-year volumes for factors which may have influenced only portions of the base year. If, for example, a rule which served to reduce mail volume was in effect for only the last two quarters of the base year, a volume-adjustment multiplier would be introduced by lowering the observed volume for the first two quarters of the base year based on the expected impact of such a rule. In this way, the base volume, adjusted by the volume-adjustment multiplier, would fully reflect the expected impact of such a rule going forward through the forecast period.

Almost all of the volume-adjustment multipliers used in the present case are constructed based on shifting some base-period volume between the Negotiated Service Agreement (NSA) portion of a particular mail subclass and the non-NSA mail categories of the same subclass.

The one exception to this is with respect to Market-Dominant Parcel Post volume. In this case, the volume-adjustment multiplier is included to adjust the base-year volume to account for a significant decline in this volume beginning around the time of the Postal Service's May, 2009, rate increase. The demand equation for Market-Dominant Parcel Post includes a dummy variable equal to one since the introduction of May, 2009, rates (D_R09). This variable has an estimated coefficient of -0.445 (t-statistic of -6.897).

Over the four quarters of the base period used in this case, this variable, D_R09, was equal to 0 in 2009Q2, had a value of (51/91) in 2009Q3, and was equal to 1 in 2009Q4 and 2010Q1. Market-Dominant Parcel Post volumes in 2009Q2 and 2009Q3 were adjusted based on what they would have been expected to be had D_R09 had a value of 1 in each of those quarters.

The mathematics of how this is done can be explained briefly as follows.

$$(1) \text{ Actual Volume} = X * e^{(D_R09 \text{ Value} * D_R09 \text{ Coefficient})}$$

$$(2) \text{ Adjusted Volume} = X * e^{(1 * D_R09 \text{ Coefficient})}$$

Re-writing (1) as a function of X and plugging it into (2), then, yields

$$(3) \text{ Adjusted Volume} = \text{Actual Volume} * [e^{(1 * D_R09 \text{ Coefficient})} / e^{(D_R09 \text{ Value} * D_R09 \text{ Coefficient})}]$$

Adjustments were made separately for inter-BMC and intra-BMC market-dominant Parcel Post. The specific adjustments made are shown in the Table below.

	<u>Volume</u>	<u>Value of D_R09</u>	<u>Coefficient</u>	<u>Adjusted Volume</u>
<u>2009Q2</u>		0	-0.444522	
Inter-BMC	17.826			11.429
Intra-BMC	5.379			3.448
<u>2009Q3</u>		(51/91)	-0.444522	
Inter-BMC	9.074			7.463
Intra-BMC	8.320			6.843
<u>2009Q4</u>		1	-0.444522	
Inter-BMC	0.000			0.000
Intra-BMC	13.045			13.045
<u>2010Q1</u>		1	-0.444522	
Inter-BMC	0.000			0.000
Intra-BMC	16.712			16.712
<u>Base Year</u>				
Inter-BMC	26.900			18.892
Intra-BMC	43.455			40.048
<u>Volume-Adjustment Multipliers</u>				
Inter-BMC				0.7023
Intra-BMC				0.9216

**Response of United States Postal Service to Request for Additional
Information
Related to Volume Forecasting from Technical Conference on July 19, 2010**

2. Hodrick-Prescott Filters

At the July 19, 2010, Technical Conference, the Postal Service was asked to provide the spreadsheet used to apply Hodrick-Prescott filters to the macro-economic data used in the volume forecasting spreadsheets filed in USPS-R2010-4/8.

The attached spreadsheet, 1st.TC.FilteredData.xlsx, calculates Trend components for Retail Sales (STRR), Employment (EMPLOY), and Investment (INVR), using the Hodrick-Prescott filter. Note that because of the complexity of the calculations here, this spreadsheet requires Excel 2007 or a later version.

The Cyclical component of these variables is calculated by subtracting the Trend component from the unadjusted data. The cumulative negative trend variables, EMPL_TN_L and INVR_TN_L, are constructed as described at pages 9 – 11 of the document “Narrative Explanation of Econometric Demand Equations for Market Dominant Products filed with the Postal Regulatory Commission on January 20, 2010”, which was filed with the Commission on July 1, 2010.

**Response of United States Postal Service to Request for Additional
Information
Related to Volume Forecasting from Technical Conference on July 19, 2010**

3. Workshare Equations

At the July 19, 2010, Technical Conference, the Postal Service was asked to provide a version of the 'Shares' sheet of the volume forecasting spreadsheets filed in USPS-R2010-4/8 which would allow one to update the share forecasts given changes to the worksharing discounts.

Unfortunately, in preparing this spreadsheet, it was discovered that the discounts used in constructing the volume forecasts originally filed with USPS-R2010-4/8 were the same in all three forecasts and that, moreover, these discounts were not entirely correct for any of the three forecasts. These errors have been corrected in the revised versions of USPS-R2010-4/8 and USPS-R2010-4/NP3 filed on July 26, 2010. The revised versions also allow one to update the share forecasts given changes to the worksharing discounts.

**Response of United States Postal Service to Request for Additional
Information
Related to Volume Forecasting from Technical Conference on July 23, 2010**

1. Lag Effects

At the technical conference on July 23, 2010, despite the fact that the same topic had been covered at the Technical Conference on July 19, 2010, a question was posed regarding the period of time over which the lagged price effects in the equation affect the forecasts. As a practical matter, a forecast through Quarter 2 of FY2012 would be sufficient to allow all of the lag effects to play out in the price variables. Technically speaking, with new rates scheduled to take effect on Sunday, January 2, 2011, there is a very small fraction of Quarter 2 of FY11 in which the "old" rates are still effective. Therefore, a minute portion of the lag effect would not show up until Quarter 3 of FY2012 but, again, as a practical matter, that can reasonably be ignored.

**Response of United States Postal Service to Request for Additional
Information Related to Cost Reduction Programs from
Technical Conference on July 19, 2010**

At the Technical Conference on July 19, 2010, interest was expressed in a description of the various cost reduction programs reflected in financial estimates provided by Mr. Masse for FY2011, akin to the types of descriptions provided in Docket No. R2006-1 as a part of Library Reference USPS-LR-L-49. The requested descriptions are attached to this response electronically as a pdf file (Ist.TC.Cost.Red.Prog.Descriptions).

Postal Regulatory Commission
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EXIGENT RATE CASE

Rate Adjustment Due to Extraordinary or Exceptional Circumstances

Docket No. R2010-4

**EXPLANATION OF COST REDUCTIONS,
OTHER PROGRAMS,
AND CORPORATEWIDE ACTIVITIES**

INTRODUCTION

This document summarizes the major programs and management initiatives expected to be active during fiscal years 2010 and 2011. It performs a similar role to the corresponding parts of Library Reference USPS-LR-L-49 in Docket No. R2006-1. The discussion of the programs and activities is organized into the three groupings briefly described below. Personnel-related and non-personnel related expenses are identified by cost component.

Cost Reduction Programs are Postal Service initiated-programs that result in cost savings. The Cost Reduction Programs are organized into two sections: cost savings programs addressing operational and other cost reductions in Section 1A, and Breakthrough Productivity Initiatives to achieve savings in addition to specific operational and other programs in Section 1B.

Other Programs add costs for initiatives related to operational and service improvement as well as security. Cost increases associated with cost reduction programs are also included. The Other Programs are identified in Section 2.

Corporatewide Activities reflect national costs initiatives affecting Headquarters and field service units. These activities are generally non-discretionary and ongoing, as opposed to programs which have a life cycle.

Each of the major programs and initiatives is subjected to an intensive review and validation by our investment review and approval process. During the formulation phase of the budget process, an additional check is performed on all major program assumptions. This step involves field and Headquarters executives who review the program savings/cost targets and resolve issues with the program managers or sponsors. These steps ensure the planning assumptions used in formulating program expectations are reasonable and accurately portray the impact a program will have on the Postal Service's financial position.

Program savings/costs reflect both new programs initiated in the current fiscal year and partial year savings/costs which carryover from the previous fiscal year.

Workhour savings/costs are estimated using the most appropriate methodology for each particular program. For major mail sortation equipment deployments, site-specific data and information concerning equipment and mail flows are used.

Feed rates, read rates, reject rates, densities, flows, etc., for the affected sortation operations are estimated to derive net workhour savings/costs.

Equipment field test data are also used in estimating program expectations.

Some types of program savings/costs are calculated using additional engineering methods studies and management's judgment from past experience. Some programs show lag times ranging from one to several months between the date

of the equipment deployment and the realization of full workhour savings/costs. Individual site savings/costs estimates are aggregated to calculate the total national program costs/savings estimate.

This means that most calculations of savings/costs takes into account local, and generally unique, conditions at each site where the program (or equipment) is going to be deployed. However, for some programs, local factors do not materially impact program expectations and average savings/costs per program (or equipment) calculations are utilized. For these programs, savings/cost projections are generally based on national averages rather than being site specific.

Section 1A

Cost Reduction Programs

739 ADDITIONAL DELIVERY BARCODE SORTERS STACKER MODULES

(EN-61)

This program provides 739 additional stacker modules and 1,478 supporting tray carts for existing DBCS Phase 2 – 6 machines at 110 postal processing facilities.

Each module consists of 16 additional sort bins that help expedite the distribution of letter mail by providing a greater depth-of-sort to existing letter mail processing operations, thereby reducing the number of handlings required to sort letter mail to its final destination.

POSTAL AUTOMATED REDIRECTION SYSTEM (PARS) - PHASE 2 (EN-105)

The Postal Automated Redirection System (PARS) handles Undeliverable-As-Addressed (UAA) letter mail more efficiently than today's process. The UAA mail is intercepted earlier in the sorting process, resulting in a reduction in total handlings.

The initial phase of the PARS program, Phase I, covered comprehensive implementation of the PARS program in 50 Postal Processing & Distribution Centers (P&DCs), all of our Remote Encoding Centers (RECs), and the delivery

units they serve. Additionally, scanners were deployed into Computerized Forwarding System (CFS) units, as appropriate, to allow a PARS database with nationwide coverage to be constructed immediately. Phase II of the program was implemented into 233 additional P&DCs and the delivery units they serve. Some CFS units lost their mechanized letter terminals; others were reconfigured as their automated letter mail workload was redirected to a nearby processing plant. The IMS version 4.0 incentive software, released in July/August 2007 has increased the weighted intercept and AFR finalization rates, and COA REC productivities resulting in additional workhour savings.

POSTAL AUTOMATED REDIRECTION SYSTEM (PARS - 3) – LETTER INCENTIVE PROGRAM (EN-88)

The PARS Letter Incentive Program provided a single PARS software release that was deployed in May 2009 and provided the following PARS performance improvements:

- 1.87% increase in Undeliverable-as-Addressed (UAA) intercept rate
- 12.33% increase in Advanced Forwarding Reader (AFR) intercept finalization rate
- 5.72% increase in AFR Carrier Identified Forward finalization rate
- 12.77% increase in AFR Return-to-Sender (RTS) finalization rate
- 48 images per hour increase in Remote Encoding Center (REC) keying productivity for UAA images

- 34 images per hour increase in REC keying for Change-of-Address (COA) form images
- 1.03% reduction in non-UAA mail intercepted incorrectly

Other benefits of this software release included:

- Supports Intelligent Mail Barcode (IMB) requirements by increasing the limits for Mailer Identification (ID) numbers from 6- to 9-digits
- Supports the national COA address database by consolidating multiple Computerized Forwarding Site (CFS) site-specific databases into a single national database
- Provides the capability to implement future rate changes via a loadable table instead of requiring a software release

Deployment of the software upgrade began on May 01, 2009 and ended May 18, 2009.

ADVANCED FACER CANCELLER SYSTEM (AFCS) IMPROVEMENTS (EN-84)

This program improves the performance of letter mail cancellation equipment by providing double feed detection and cancellation upgrades for all 1,086

Advanced Facer Canceller System (AFCS) machines. The double feed detector will recognize double feeds as they occur and create a more efficient mail handling process. The inkjet printer will automate the AFCS cancellation process from the current manual method.

These enhancements will increase the efficiency of letter mail processing operations by reducing remote keying requirements, decreasing the amount of mail that has to be rehandled manually due to miscoding by the AFCS, and eliminating the manual effort required to update the AFCS machine's cancellation date stamp. Maintenance costs will also be reduced.

AUTOMATED LETTER MOVEMENT SYSTEM

The Automated Letter Movement System (ALMS) will connect multiple Advanced Facer Canceller Systems (AFCS) to multiple Delivery Bar Code Sorters (DBCS).

It will allow mail processed by multiple AFCS/ISSs to be routed directly to multiple DBCS/OSSs.

The ALMS will eliminate manual sweeping of the AFCS stackers and movement of mail in trays from the AFCS to downstream operations by mail handlers (LDC-17), as well as significantly reduce the manual feeding of mail into the DBCS/OSS by mail processors (LDC 11). This program will also improve customer service by increasing mail quality and reducing mail processing time through implementation of a continuous flow (from AFCS to DBCS) process.

DISTRIBUTION QUALITY IMPROVEMENT – PHASE 1 PROGRAM (EN-102)

The Distribution Quality Improvement (DQI) Program is enhancing the address

recognition technology used in letter mail automation equipment. This program is encoding much of the letter mail that cannot be barcoded or can only be partially barcoded to a finer depth of code, and sorted to delivery points.

Increases in acceptance and finest depth of sort rates reduce keying workhours required at Remote Encoding Centers (RECs) and manual distribution workhours at plants and delivery units. Lower RCR error rates produce workhour savings in manual distribution and carrier casing.

DISTRIBUTION QUALITY IMPROVEMENT (DQI) – PHASE 2 (EN-86)

The DQI Phase 2 Program is enhancing the address recognition technology used in letter mail automation equipment. This is the second phase of an incentive-based program that is improving Remote Computer Reader (RCR) encode rates and reducing error rates through the use of a commercially available name and address database. The following improvements are targeted under this program:

- 0.20 percentage point increase in the RCR accept rate
- 1.65 percentage point increase in RCR finest depth of sort rate
- 0.50 percentage point reduction in RCR error rates

The plan included four incremental software releases from April 2009 – August 2011.

110 ADDITIONAL DELIVERY BARCODE SORTERS PHASE 6 (DBCS 6) AND 394 ADDITIONAL STACKER MODULES (EN-50)

This program provides 110 new Delivery Barcode Sorter Phase 6 machines (DBCS-6) and 394 additional stacker modules for existing DBCS Phase 2 – 5 machines. The new DBCS equipment is used to increase the amount of letter mail that can be processed in automated operations. It provides additional capacity needed to increase delivery point sequenced volumes. The number of sort bins provided for each new machine is specific to the respective facility's requirements.

Each stacker module consists of 16 additional sort bins that help expedite the distribution of letter mail by providing a greater depth-of-sort and a reduction in the number of total piece handlings. The additional stacker modules increase the number of firm holdouts available during DPS operations.

DELIVERY BAR CODE SORTER (DBCS) CENTRAL VACUUM SYSTEMS (EN-101)

The DBCS Central Vacuum System program is installing 1,307 centralized vacuum systems to maintain 4,427 DBCS machines (Phase 2 through 5) at 480 postal facilities. Each central system consists of a heavy duty vacuum unit and a network of steel tubing connected to a group of up to four DBCSs. Debris is deposited at a central location. The central vacuum unit is mounted on heavy-duty wheels and can be easily moved and re-located within the plant. This

program will reduce the maintenance workhours required to service the DBCSs.

This program will also provide parts savings due to elimination of the multiple bags and filters used in the existing portable systems and longer motor life expectations in the central vacuum systems.

CENTRAL VACUUM SYSTEMS FOR PHASE 1 DELIVERY BAR CODE SORTER (DBCS) MACHINES (EN-51)

The Central Vacuum Systems for Phase 1 Delivery Bar Code Sorter (DBCS) Machines program will install 227 centralized vacuum systems to maintain 676 existing Phase 1 DBCS machines located at 129 postal facilities. Each system consists of a heavy duty vacuum unit and a network of steel tubing connected to a group of up to four DBCSs. Debris is deposited at a central location. The central vacuum unit is mounted on heavy-duty wheels and can be easily moved and re-located within the plant. This program will reduce the maintenance workhours required to service the DBCS Phase 1 machines.

DBCS 7 MACHINES

Currently under further review. This program would provide new Delivery Barcode Sorter machines.

AFSM 100 CANCELLATION UPGRADE PROGRAM (EN-87)

This program purchased 230 AFSM 100 cancellation upgrade kits (227

operational and 3 training/support systems) that allowed cancellation of First-Class flat mail on the AFSM 100. The program reduced flat mail processing costs by significantly reducing the need to process flats on stand-alone cancellation machines or via hand cancellations.

FUTURE FLAT SEQUENCING SYSTEM

This program is currently undergoing further evaluation. The Flats Sequencing System (FSS) will be used to walk sequence flat mail pieces that are to be delivered within one or more 5-digit delivery zones. The FSS machine will have 360 sortation bins and flat mail pieces will be passed through it twice, resulting in flats in walk sequence for each letter carrier.

The first 100 FSS machines are being deployed under the BOG approved FSS Phase 1 Program. This program would cover additional deployments beyond Phase 1.

FLAT RECOGNITION IMPROVEMENT PROGRAM (FRIP) PHASE 2 (EN-103)

Phase 2 of the Flat Recognition Improvement Program (FRIP) will provide additional enhancements to the address recognition technology used in flat mail automation equipment. This program will improve optical character reader (OCR) accept rates and reduce OCR error rates on all AFSM 100 and UFSM

1000 equipment.

Increases in the AFSM 100 OCR accept rate will reduce keying workhours at Remote Encoding Centers, while a higher UFSM 1000 OCR accept rate will decrease UFSM 1000 keying or manual flat sorting workhours in our plants. Lower OCR error rates will produce workhour savings in manual flat sorting and carrier operations.

FLATS SEQUENCING SYSTEM (FSS) RESEARCH & DEVELOPMENT ENGINEERING(EN-107)

The Flats Sequencing System (FSS) will be used to walk sequence flat mail pieces that are to be delivered within one or more 5-digit delivery zones.

Under this R&D project, one PreProduction FSS machine will be installed in the Dulles VA P&DC. It will be a full-sized FSS that is expected to have 360 sortation bins and all of the functionality of the FSSs that subsequently will be deployed. Flat mail pieces will be passed through it twice, resulting in flats in walk sequence for each letter carrier.

Following the completion of the Postal Service's field acceptance test, a one year operational test will be conducted, frequently with live mail, with postal employees staffing the machine.

FLATS SEQUENCING SYSTEM (FSS) – PHASE 1 (EN-108)

The Flats Sequencing System (FSS) will sort flat-sized mail into delivery sequence at high speeds and at a much higher productivity than today's manual process. The FSS will process flats from the AFSM 100 and UFSM 1000 mail streams along with a significant amount of carrier presorted mail that is not handled on our automation equipment today.

The production FSS machine will have 360 sortation bins and flat mail pieces will be passed through it twice, resulting in flats sorted to walk sequence for each letter carrier. The FSS Phase 1 program will deploy 100 FSS machines.

Savings are expected to result in a reduction in carrier workhours , carrier supervisor hours , and delivery unit clerk hours as a portion of our flat mail arrives at the delivery units in walk sequence order. For the portion of flats that can be processed on the FSS, the manual casing and pull-down activities will no longer be necessary.

FIELD MATERIAL HANDLING SYSTEMS(EN-75)

Material Handling Systems are being deployed to support material handling operations in our plants, Bulk Mail Centers (BMCs), and Air Mail Centers (AMCs). The primary goal is to reduce LDC-17 labor hours associated with the

handling of all types of mail by providing better material handling solutions and system modifications to the facilities.

This program is being implemented through a series of individual, site-specific projects initiated by requests from the plants, or identified through proactive site staff.

PACKAGE RECOGNITION IMPROVEMENT PROGRAM – PRIP (EN-106)

The Package Recognition Improvement Program (PRIP) will upgrade the address recognition capabilities of the 76 Phase 1 Automated Package Processing System (APPS) machines that have been purchased. This program will improve the efficiency of parcel and bundle sorting operations by reducing the amount of mail that requires remote keying support at the Remote Encoding Centers (RECs) that process APPS images.

The upgrades consist of three incremental software releases over a three-year period. All of the savings expected from this program are at the Remote Encode Centers. The savings are based on incremental improvements in OCR recognition capabilities for the Phase 1 APPS machines.

CENTRAL VACUUM SYSTEMS FOR AUTOMATED FLAT SORTING MACHINE (AFSM) 100s (EN-85)

This program deployed centralized vacuum systems for all Automated Flat

Sorting Machine (AFSM) 100 equipment. A total of 534 centralized central vacuum systems, one for each AFSM, were purchased as replacements for the costly portable vacuums previously used. A total of 530 of the 534 systems purchased were deployed and installed. The remaining systems are being held at Topeka. Deployment began in February 2009 and was completed in November 2009.

PHILADELPHIA NETWORK DISTRIBUTION CENTER (NDC) – (EN89)

This program cover the work required to allow the Philadelphia NDC to process the originating Priority Mail flats and parcels being relocated from the P & DC due to its planned closure when the lease expires in March 2010. The project includes demolishing two Parcel Sorter Machines and two Sack Sorter Machines and relocating the control room and computer room. In addition, a 200 bin Automated Package Processing System (APPS) will be transferred from another site and a Small Parcel and Bundle Sorter (SPBS) and SPBS feed system will be removed.

SURFACE VISIBILITY (NO-01)

The Surface Visibility system collects information and reports on asset tracking, providing visibility into the movement of each sack, tray, container, and trailer within the USPS supply chain. This kind of real-time visibility affords the Postal Service the opportunity to identify problems such as:

- Mail that was processed late, resulting in a container missing its assigned dispatch.

- Handling units that were loaded into the wrong containers and containers loaded onto the wrong trailers.

AUTOMATED PACKAGE PROCESSING SYSTEM (APPS) – SORT ACCURACY IMPROVEMENT (SAI) PROGRAM

The APPS Sort Accuracy Improvement Program (SAI) upgraded all 74 existing Automated Package Processing System (APPS) machines with Sort Accuracy Improvement kits. This enhancement reduces sorting errors resulting in improved service for mail processed on the APPS.

Deployment of all 129 operational kits and 2 training/support kits began on June 30, 2009 and ended November 18, 2009. Each of the 55 dual induction APPS machines received two (2) SAI kits (one per induction station); and each of the 19 single induction machines received one (1) SAI kit.

REMOTE ENCODING CENTER (REC) CONSOLIDATIONS

As the technology for computerized resolution of addresses improves, the percentage of mail requiring manual keying at the RECs is reduced. Currently, the reduction of keying requirements due to improvements in computerized encoding is being offset by additional keying requirements for other products such as flat mail, Automated Package Processing Systems (APPS) and the

Postal Automated Redirection System (PARS). Although the keying requirements for each are different, and they are handled in separate operations, the Postal Service is pursuing their integration.

MULTI-CHANNEL CUSTOMER EXPERIENCE IMPROVEMENT PROJECT (HR03) -- PROJECT PHOENIX

Project Phoenix will address increasing competitive and technological challenges by improving the underlying information technology (IT) that supports three key revenue generating channels within USPS: the website (USPS.com), the contact center, and retail. Project Phoenix will also fund enhancements to USPS.com and the contact centers. These improvements will support a more positive and consistent customer experience across channels by offering more products and services, and will positively impact customer satisfaction, retention, and revenue growth. The improvements will also reduce IT maintenance and integration costs over time.

Project Phoenix will be implemented in two phases and multiple releases. Revenue growth is anticipated due to Project Phoenix. This project will generate an increase in revenue primarily by enhancing the customer experience through the Internet channel and contact centers. Enhancements to the website will make it easier for customers to find the products they need by creating a more streamlined and intuitive user interface. Customer data integration between the

contact center and Internet channels will promote customer satisfaction by enabling agents to provide consistent personal service.

The redirection of Shipping and Stamps revenue from the retail channel to USPS.com will result in cost savings and cost avoidance due to a reduction in retail staffing hours.

LEARNING MANAGEMENT SYSTEM (HR-02)

The Learning Management System is a comprehensive learning solution that will enable the Postal

Service to manage and integrate a full range of its training, administration, delivery, and talent management processes. Currently, these processes are managed using multiple legacy systems that lack interoperability and are inefficient and costly to maintain.

The LMS system includes an intuitive learning portal and learning management software, as well as test authoring, content structuring, content management, and collaboration functionality. The system offers back-office functionality for competency management and comprehensive support of performance management. It provides strong analytical functionality that includes support for ad hoc reporting. The LMS tailors learning paths to an individual's educational

needs and personal learning style. This personalized learning that is based on job requirement, tasks preferences, and existing knowledge improves learning efficiency for employees by providing the training needed for their development.

Section 1B

Breakthrough Productivity Initiatives (BPI)

Breakthrough Productivity Initiatives (BPI) refer to various initiatives and actions by the Field and Headquarters to achieve savings in addition to specific operational programs. The savings are achieved through implementation of standardized field operations procedures and information systems resulting in increased efficiencies in operational functions, reductions in administrative functional areas, and more efficient transportation utilization. The improved processes enable the Postal Service to develop specific measures of performance and national targets, and support the Transformation Plan goal of better aligning workhours to workload.

In Fiscal Year 1999, efforts were underway to develop and establish a mechanism that would fairly measure the performance for plant and delivery Operations. From this effort, the Breakthrough Productivity Initiative (BPI) was developed and implemented.

The Breakthrough Productivity Initiatives for Mail Processing, Customer Service, and Delivery Services are a tool used to measure production efficiency. This is accomplished by collecting data (volume and actual hours) by processing category type, (e.g. automation or manual, office or street delivery).

The Performance Achievement measure is the computed value that corresponds to the production efficiency for a unique operation and is represented as a percent value, 0% to 100%, with 100% representing the highest. The Performance Achievement Percent is computed as follows:

- Total Mail Volume by unique category - Actual
- Total Work Hours by unique category - Actual
- Predefined Target Productivity – Computed yearly based on actual productivity by category
- Earned Hours – Computed value based on Total Mail Volume divided by Predefined Target Productivity
- Opportunity Hours – Computed value based on Total Work Hours minus Earned Hours

Although opportunity hours are calculated for each type of operation, it is unlikely that field initiatives will result in the same percentage reduction in opportunity hours for each type of operation. Since savings estimates are more predictable for larger groups of operations, BPI savings are assumed distributed to each of the following groups in direct proportion to the opportunity hours in each group.

- Letter Distribution such as the Delivery Barcode Sorter (DBCS) and manual letter casing.
- Flats Distribution such as the Advanced Flats Sorting Machine 100 (AFSM 100) and manual flats casing.
- Bulk Mail Centers

- Manual Priority and Parcels
- Other Mechanized operations such as the Small Parcel and Bundle Sorter (SPBS) and the Tray Sorter

The Breakthrough Productivity Initiative for Maintenance currently encompasses two efforts. The first initiative focuses on improving the performance of the custodial staffs and monitoring performance using workhours per 1,000 square feet of interior and exterior space. The second initiative focuses on reducing the replenishment costs of maintenance spare parts and supplies in field maintenance stockrooms by comparing actual inventory value with the inventory value that would exist at two inventory turns per year.

Section 2

Other Programs

Most programs add costs as well as generate savings. The cost portion is called and labeled "Other Programs". The following programs include identified costs, as well as cost savings, during the period. For program descriptions, see Section 1A, Cost Reduction Programs.

- AUTOMATED LETTER MOVEMENT SYSTEM (ALMS)
- DELIVERY BAR CODE SORTER CENTRAL VACUUM SYSTEMS
- CENTRAL VACUUM SYSTEMS FOR PHASE 1 DBCS'S
- DBCS 7 MACHINES
- CENTRAL VACUUM SYSTEMS FOR AFSM 100 MACHINES
- AFSM 100 CANCELLATION UPGRADE
- PHILADELPHIA NETWORK DISTRIBUTION CENTER
- FUTURE FLAT SEQUENCING SYSTEM (FSS)
- FLATS SEQUENCING SYSTEM PHASE 1
- FIELD FIXED MECHANIZATION /FIELD MATERIAL HANDLING
SYSTEM (CURRENT&FUTURE)
- APPS SORT ACCURACY IMPROVEMENT

Section 3

Corporatewide Activities

EXPEDITED MAIL SUPPLIES & SERVICES

This activity is intended to cover printing of Express Mail and Priority Mail envelopes, boxes, labels, forms, and tags.

ADVERTISING

The advertising program provides information on our products and services using the following media: television, radio, outdoor, transit, magazines, newspapers, direct mail and newsletters, film and video, yellow pages, post office lobby posters and displays, and promotional materials such as posters, brochures, and point-of-purchase items.

RESEARCH & DEVELOPMENT

Corporatewide activities include research and development which have the objectives of improving service, reducing costs, and providing an adequate working environment by implementing new and improved technology-based

systems. These systems affect practically all areas of the postal system, including mail processing, transportation, delivery, retail services, administrative services, and new postal products. Many cost reduction program savings are based on new and improved technology-based systems resulting from Research and Development.

ALL OTHER CORPORATEWIDE ACTIVITIES

This item reflects the estimated change in expenses for corporatewide activities that have not been listed separately (i.e., activities that are centrally funded and managed, such as debit/credit card, mail transport equipment and postage stock).

**Response of United States Postal Service to Request for Additional
Information Related to Cost Reduction Programs from
Technical Conference on July 27, 2010**

At the Technical Conference on July 27, 2010, further interest was expressed in a presentation breaking out estimated cost savings by program as the product of workhour savings and productive hourly rates, also akin to part of USPS-LR-L-49. That breakout is attached to this response electronically as 3rd.TC.Cost.Redctn.Attach.xls.

With regard to the source of the workhour savings estimates, those estimates generally start with the estimates in the Decision Analysis Report (DAR), if a DAR has been completed. If not, estimates would need to be developed separately. After a program is implemented, as events unfold, DAR estimates may be adjusted for variances, primarily due to schedule changes. For example, estimates used in the budget for a subsequent year may not necessarily match initial estimates in the DAR for that subsequent year.

Thus, the workhour savings estimates upon which the cost reduction program portion of Mr. Masse's presentation is premised may involve both the original workhour estimates in the DAR, plus ongoing consultations between program managers, Operations, and Finance.

Response of United States Postal Service to Request During
Technical Conference on July 27, 2010
for Additional Information Related to Flats Strategy Programs

At the Technical Conference on July 27, 2010, interest was expressed on when the 30 operational strategies might be implemented, and the firmness of our expectations that any particular item might be among those implemented. Responsive information is provided in the following chart.

	OPERATIONS	Size of Opportunity	Development Stage [a]	Savings Expected [b]
	Transportation			
1	Improving Handling Unit/Container Density	Large	Concept	2011
2	Eliminate Periodical and Standard Mail Flown	Small	Concept	2011
3	Transportation Utilization (all products)	Large	Development	2011
4	Network Optimization (all products)	Medium	Development	2011
	Mail Processing			
5	Facility Optimization	Large	Development	Ongoing
6	Equipment optimization	Medium	Development	2012
7	Future FSS enhancements and processing modes	Medium	Concept	2012 or later
8	Automated Flats Preparation (AFP)	Medium	Concept	2013 or later
9	Automated Package and Bundle Sorter	Medium	Planning	Ongoing
10	Material Handling	Large	Planning	2011 or later
11	Flat Recognition Improvements	Small	Development	2011
12	Automated Flats Forwarding	Small	Concept	2013 or later
13	Using IMb data to determine letters processed on flat sorting equipment	Small	Concept	2011 or later
14	Electronic Condition-Based Maintenance	Small	Development	2011
15	Utilize a single Incoming Secondary run for all flats	Small	Concept	2011 or later
16	Monthly Periodicals – merge with Standard Mail service standards	Sm/Med	Concept	2011 or later
17	Distribution compression (all products)	Large	Planning	2011
18	Reduce mixed-states consolidation processing locations (L009) and optimize mixed states flow	Medium	Development	Ongoing
19	Realign operating and transportation plan to improve utilization	Medium	Concept	Ongoing
20	Periodicals Lean Six Sigma (LSS) end-to-end value stream mapping project	Undefined	Concept	Ongoing

Response of United States Postal Service to Request During
Technical Conference on July 27, 2010
for Additional Information Related to Flats Strategy Programs

21	Refine work methods to improve Business Mail Entry Unit (BMEU) / Plant load handoff to mail processing	Large	Concept	Ongoing
22	Sort Plan Optimization (SPO) for flats	Small	Development	Ongoing
23	Continuous Improvement	Undefined	Concept	Ongoing
Post Office and Delivery Operations				
24	Business Plan Staffing and Scheduling Reviews	Large	Planning	Ongoing
25	Shifting distribution from Post Office Operations (Function 4) to Mail Processing Operations (Function 1)	Medium	Planning	Ongoing
26	Customer Service Unit Optimization	Medium	Concept	2011 or later
27	FSS work methods	Large	Development	Ongoing
28	Route Adjustments - Joint Alternate Route Assessment Process (JARAP) / Carrier Optimal Routing (COR) (all products)	Medium	Development	Ongoing
29	Route Optimization 100 Percent Street routes	Large	Concept	2011
30	Facility Optimization (all products)	Small	Development	Ongoing

[a] *Concept* indicates that an opportunity has been identified, but no plan has yet been developed to take advantage of it.

Development indicates that a plan is being identified to take advantage of an opportunity.

Planning indicates that planning for implementation of a plan is taking place.

[b] This is the earliest date that savings from an opportunity can be expected.

DOCKET NO. R2010-4
INSTITUTIONAL RESPONSES TO
PRESIDING OFFICER'S INFORMATION REQUESTS

<u>POIR</u>	<u>Question</u>
POIR No. 1	1
POIR No. 3	20-23
POIR No. 4	5, 9

**RESPONSE OF THE UNITED STATES POSTAL SERVICE
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 1**

1. Please refer to Library Reference USPS-LR-9, Operations Plans for Flats. The Postal Service discusses 29 strategies for improving transportation, mail processing, and Post Office operations and delivery. Also, please refer to the attached Excel worksheet "Flats strategy.xlsx" as an example of the level of detail being sought in the following questions.

- a. For each of these strategies, please provide a quantitative estimate of each program's overall impact on cost. Please utilize the most recent existing information (such as Decision Analysis Reports or Return on Investment calculations) in responding and identifying the sources relied on.
- b. Please provide the unit cost savings from each strategy for Periodicals and Standard Mail Flats for FY 2010 through FY 2013.
- c. For each unit cost savings in subpart a., please provide detailed information for each affected cost segment or cost pool to support the estimate of unit cost savings. Details should be as specific as possible (e.g., percent increase in productivity and/or changes in machine throughput.)
- d. Please calculate an estimated unit cost based on the savings from subpart b. for Standard Mail Flats and Periodicals for FY 2010 through FY 2013.
- e. Please provide the estimated cost coverage for Standard Mail Flats and Periodicals for FY 2010 through FY 2013 using the projected unit cost calculated in subpart d.
- f. If the cost coverage does not exceed 100 percent for Standard Mail Flats or Periodicals by FY 2013, please explain when the product in question is estimated to cover its cost and describe additional steps to be taken to achieve profitability.

RESPONSE:

All programs for which cost savings have been planned or budgeted are contained in Mr. Masse's statement and associated materials. Beyond these programs, cost savings are more speculative; they are based on the size of the opportunity, but detailed plans for addressing each issue have not all been developed yet. Additional savings from the strategies in USPS-R2010-4/9 are part of the Postal Service's productivity goals, and are recognized in the BPI provisions of Mr. Masse's estimates.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

20. The following questions concern potential transportation savings identified in the Flats Strategy, USPS-R2010-4-LR-9. These improvements are estimated to be implemented during the test year

- a. Please provide the percentage of Flats that currently utilize the NDC network.
- b. When will the Redesign of NDC Mail Transportation Equipment (MTE) be completed?
- c. Please provide the estimated ROI for this project.
- d. When will the NDC/Surface Transportation Center Integration be completed?
- e. Please provide the estimated ROI for this project.

RESPONSE:

- a. No estimate of this percentage has been identified.
- b. 2011
- c. No ROI for this project is currently available because cost estimates for new equipment associated with it have not been finalized
- d. 2012
- e. Expected savings for all mail is \$125 million; no additional investment is expected.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

21. The following questions concern the estimated savings from the implementation of the FSS provided in USPS-LR-R2010-4-NP-2:

- a. Please provide the total amount of cost savings estimated for the FSS in FY 2010 and FY 2011.
- b. Please provide the source and methodology for that estimate.
- c. USPS OIG Audit DA-AR-10-007, concerning the performance projection of the FSS in the FY 2010 Q1 *Investment Highlights*, states that the estimated savings from the FSS machines do not comport with the DAR methodology or current performance. How does the methodology described in subpart b. differ from the methodology used in the Q1 FY 2010 *Investment Highlights*.

RESPONSE:

- a. Savings related to FSS are detailed in the attachment to the Response of the United States Postal Service to Informal Question Regarding Cost Reduction Programs Posed at the Technical Conference on July 27, 2010 (3rd.TC.Cost.Redctn.Attach.xls, filed August 2, 2010). The information requested can be found in rows 24-27 of the first four worksheets contained in the file.
- b. The cost savings estimate is based on internal Postal Service projections of machine performance, which are in turn driven by flat mail volume projections and the FSS deployment schedule.
- c. The methodology described in subpart b is essentially the same as the Investment Highlights methodology. The range of expectations contained in the Q1 FY 2010 Investment Highlights projects a range of possibilities which varies machine throughput, and also includes benefits from the use of Transitional Employees during the implementation period.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

22. According to the Flats Strategy, USPS-R2010-4-LR-9, the estimated date of implementation for the programs listed below is after FY 2011. For each program, as available, please provide the following: (1) a description of the concept; (2) when the decision to implement the concept will be made; and (3) any available additional detail concerning cost savings estimates for:

- a. Automated Flats Preparation;
- b. Automated Package and Bundle Sorter;
- c. Material Handling;
- d. Utilize a single Incoming Secondary run for all flats;
- e. Route Optimization 100 Percent Street Routes; and
- f. Facility Optimization.

RESPONSE:

Beyond the description in the original document, details on the practical scope or implementation of these concepts relies on a number of factors, including feasibility, the cost and effectiveness of new equipment, and negotiations with the unions. Any decision to develop a program will be dependent on evaluations of these factors, which do not themselves have timelines for completion.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

23. According to the Flats Strategy, USPS-R2010-4-LR-9, the estimated date of implementation for the programs identified below occurs before or during FY 2011.

a. Equipment Optimization

- i. Please provide the percentage of bundles currently processed in a non-optimal fashion on the SPBS or manually.
- ii. Please provide the FY 2009 APPS operational run-time availability, excluding maintenance time.
- iii. Please provide the FY 2009 APPS run-time.
- iv. Please provide the percentage of pieces currently processed in a non-optimal fashion by manual sort.
- v. Please provide the FY 2009 AFSM operational run-time availability, excluding maintenance time.
- vi. Please provide the FY 2009 AFSM run-time.

b. Reduce mixed-states consolidation processing locations (L009) and optimize mixed-states flow

- i. Please provide the current cost of the L009 operation.
- ii. When will consolidation be completed?
- iii. What will be the effect on service of consolidation?
- iv. Please provide the savings from consolidation.

c. Realign operating and transportation plan to improve utilization

- i. Please provide the current nationwide standard for Critical Entry Times.
- ii. Please provide the percentage of mail tendered after the Critical Entry Time.

d. Shifting distribution from Post Office Operations (Function 4) to Mail processing Operations (Function 1)

- i. Please provide the percentage of mail currently processed in Function 4.
- ii. Please provide or discuss the Postal Service's plan for centralizing the processing of flats to Function 1.

RESPONSE:

- a. i. Unknown. The Postal Service does not track bundle mail that is processed annually.
- ii. 371,287 hours
- iii. 309,512 hours

**RESPONSE OF THE UNITED STATES POSTAL SERVICE
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 3**

- iv. 30 percent of volume was handled manually in FY 2009.
 - v. 2,484,195 hours
 - vi. 1,669,821 hours
- b. i. The annual cost of single-piece processing of outgoing mixed states residue flat volumes entered under the L009 labeling list is estimated at \$8.4 million
- ii. The consolidation of mixed states residue flat distribution is expected to be complete in Quarter 2 of FY 2011
- iii. The Postal Service expects that service for these volumes will improve through a combination of streamlined mail flows and reduced cycle time for origin processing.
- iv. The savings associated with this consolidation effort is estimated for the next ten years at \$28 million each year.
- c. i. The only current nationwide standard CET is 4:00 p.m. for destinating Standard Mail
- ii. This data to provide an estimate are not recorded.
- d. i. Approximately 25.5 percent
- ii. The Postal Service is continuously researching the centralizing of flat mail distribution to locations where automated equipment capacity currently exists or redeploying excess automated equipment to locations where opportunity volume is identified. This would include mail from Function 4 distribution operations being moved to Function 1 when there is available capacity within service responsive operational windows.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE
TO PRESIDING OFFICER'S INFORMATION REQUEST NO. 4**

5. Please refer to the Flats Strategies described in USPS-LR-9. Please confirm that in addition to reducing costs for flat-shaped mail, the USPS-LR-9 strategies in the areas listed below will, if implemented, reduce the costs of parcels in general and the costs of Standard Mail NFMs/Parcels in particular. If not confirmed, please identify which of the listed strategies will, if implemented, reduce parcel costs.

- a. Transportation
 - i. Improve Handling Unit/Container Density
 - ii. Eliminate Periodical and Standard Mail Flown
 - iii. Transportation Utilization
 - iv. Network Optimization
- b. Mail Processing
 - i. Facility Optimization
 - ii. Equipment Optimization – APPS Utilization
 - iii. Automated Package and Bundle Sorter
 - iv. Material Handling
 - v. Electronic Condition-Based Maintenance
 - vi. Distribution Compression
 - vii. Realign Operating and Transportation Plan to Improve Utilization
 - viii. Refine Work Methods to Improve Business Mail Entry Unit
BMEU)/Plant Load Handoff to Mail Processing
 - ix. Continuous Improvement
- c. Post Office and Delivery Operations
 - i. Business Plan Staffing and Scheduling Reviews;
 - ii. Shifting distribution from Post Office Operations (Function 4) to Mail
Processing Operations (Function 1);
 - iii. Customer Service Unit Optimization
 - iv. Route Adjustments Joint Alternate Route Assessment Process
(JARAP) / Carrier Optimal Routing (COR)
 - v. Route Optimization 100 Percent Street Routes
 - vi. Facility Optimization

RESPONSE:

Confirmed. The strategies listed above would be expected to generate savings for parcels. Most of them, with the exception of APPS utilization and the automated package and bundle sorter, would be expected to generate savings for letters as well.

**RESPONSE OF THE UNITED STATES POSTAL SERVICE
TO PRESIDING OFFICER'S INFORMATION REQUEST NO 4**

9. Please provide the number of post offices (excluding stations and branches) that were supervised by an employee other than a permanently assigned postmaster as of the beginning of FY 2008, FY 2009 and FY 2010.

RESPONSE:

At the beginning of FY09, our best estimate is that 1,679 out of 26,928 post offices reporting workhours did not have a permanent postmaster, while at the beginning of FY10, we estimate that 3,248 out of 26,872 post offices did not have a permanent postmaster. Analysis to develop a similar estimate for the beginning of FY08 is ongoing, and an updated response will be filed if the information can be estimated using available information.

1 CHAIRMAN GOLDWAY: Is there any additional
2 information that you have for us?

3 (No response.)

4 CHAIRMAN GOLDWAY: If not, Mr. Koetting,
5 will you identify the next Postal Service witness?

6 MR. RUBIN: I'm David Rubin. I'll be
7 representing the Postal Service today, along with Mr.
8 Koetting.

9 CHAIRMAN GOLDWAY: Welcome, Mr. Rubin.

10 MR. RUBIN: Presiding Officer's Ruling No. 3
11 requested that the Postal Service make available an
12 individual to respond to questions on the Postal
13 Service's flat strategy, and in response to that
14 ruling the Postal Service calls Frank Neri to the
15 stand.

16 CHAIRMAN GOLDWAY: Mr. Neri, will you rise?
17 Whereupon,

18 FRANK NERI

19 having been duly sworn, was called as a
20 witness and was examined and testified as follows:

21 EXAMINATION BY THE COMMISSION

22 CHAIRMAN GOLDWAY: Thank you. Mr. Neri,
23 you've been offered by the Postal Service as someone
24 with knowledge to answer Commission questions relating
25 to the Postal Service's flat strategy.

1 As a foundation for your testimony here
2 today, would you please discuss your role in putting
3 together the various programs identified as being part
4 of the flat strategy?

5 THE WITNESS: Madam Chairman, as one of the
6 operations managers of Postal Service Headquarters I
7 was involved in the development of the strategies, the
8 document including the strategies. It was a
9 collective effort of various departments within
10 Operations, and collectively we assembled the document
11 for submission.

12 CHAIRMAN GOLDWAY: How many people were on
13 the team that you worked with to develop it?

14 THE WITNESS: Various managers from various
15 departments in Headquarters Operations.

16 CHAIRMAN GOLDWAY: How many is various?

17 THE WITNESS: Engineering, Delivery
18 Operations, Processing Operations are among those that
19 provided information for the document.

20 CHAIRMAN GOLDWAY: So three people
21 participated with you?

22 THE WITNESS: And their collective staff.

23 CHAIRMAN GOLDWAY: So those three
24 departments and their collective staff.

25 THE WITNESS: And Operations support

1 functions.

2 CHAIRMAN GOLDWAY: Did anyone from the field
3 attend these meetings?

4 THE WITNESS: Not that I'm aware of.

5 CHAIRMAN GOLDWAY: Did you visit the field
6 at all to see the flat sorting operations in action
7 while you were considering the --

8 THE WITNESS: Madam Chairman, yes. From my
9 perspective over many years of experience and also
10 observing our operations, I visit the field quite
11 frequently and visit with operations managers and
12 interact with operations managers on a regular basis.

13 CHAIRMAN GOLDWAY: I have several questions
14 here that have been submitted by outside parties.
15 I'll begin with some of those. This is from Valpak to
16 Masse Question 6.

17 In response to POIR No. 1, Question 1,
18 concerning cost savings from the programs in the flat
19 strategy, the Postal Service stated: All programs for
20 which cost savings have been planned or budgeted are
21 contained in Mr. Masse's statement and associated
22 materials.

23 For which programs contained in the flat
24 strategy did you provide information for Witness
25 Masse's workpapers?

1 THE WITNESS: Madam Chairman, are you
2 referring to the roll forward document, the programs
3 included in the roll forward document?

4 CHAIRMAN GOLDWAY: I believe I am.

5 THE WITNESS: Madam Chairman, the best way
6 for me to answer that question is to describe our
7 process for program development within the Postal
8 Service.

9 There's a process whenever there is a
10 decision analysis prepared and circulated, it's
11 circulated within the various functions in Postal
12 Service Headquarters and we do have input. Many of
13 these programs, the actual documents may be prepared
14 by Engineering and processed through the various
15 functions for review and input and the assumptions
16 that are made within the opportunities that are
17 described for the various programs.

18 So we have input on an ongoing basis as they
19 are developed for many of those programs and also
20 there is a process for review before it goes to our
21 funding committees within the organization for
22 approval of funding. So I would say that a number of
23 these programs -- many, if not most or all -- we do
24 have input of review and/or direct input of the
25 assumptions that are made for opportunities.

1 CHAIRMAN GOLDWAY: So not necessarily all of
2 them. You can't identify which one?

3 THE WITNESS: Many of these are over a long
4 period of time, so I would say that all of the
5 programs that are associated with decision analysis
6 are circulated through my department for review.

7 CHAIRMAN GOLDWAY: The flat strategy does
8 not contain programs that were included as line items
9 in the Masse workpapers?

10 THE WITNESS: The flat strategy does include
11 line item programs, two line item programs that are in
12 the Masse document, and they are the FSS Program and
13 the Flat Recognition Improvement Program.

14 CHAIRMAN GOLDWAY: Do you have a dedicated
15 team for a long-term flat strategy and some
16 designation of areas so that those decision analyses
17 that are circulated related to flats come to you and a
18 particular group of people?

19 THE WITNESS: It would be the responsibility
20 of my functional managers within the various
21 departments of my organization to review. They all
22 are responsible for reviewing decision analysis
23 reports, various areas of --

24 CHAIRMAN GOLDWAY: And the flat strategy is
25 not separated out into some --

1 THE WITNESS: No.

2 CHAIRMAN GOLDWAY: -- group of people?

3 THE WITNESS: No. I have a Manager of
4 Processing Operations, Processing Center Operations,
5 that's responsible for all processing center policies
6 and activities. I have a Manager of Network
7 Distribution Center Operations that has areas of
8 responsibility with respect to any initiatives that
9 are identified or developed. I have a Manager of
10 Technical Systems and Systems Integration with similar
11 responsibilities.

12 So the opportunities and initiatives are
13 circulated and/or developed through the various
14 managers.

15 CHAIRMAN GOLDWAY: Okay. I'll go back to
16 ValPak now. The question was:

17 The program automated package and bundle
18 sorter would upgrade the small parcel and bundle
19 sorter with a bar code reader, saving keyer work
20 hours. This program is defined as "in planning," the
21 furthest along stage. When will this piece of
22 equipment begin deployment, and how many SPBS will be
23 upgraded?

24 THE WITNESS: Madam Chairman, this
25 particular program is in the development stage and

1 evaluation, and that's in fact what is part of the
2 determination is based on the opportunity that has
3 been identified.

4 First, the valuation of the costs associated
5 with that conversion of the equipment and the analysis
6 on the work hour savings opportunity related to that
7 would all determine the extent of the investment and
8 the amount of equipment.

9 CHAIRMAN GOLDWAY: So in the development
10 stage you are analyzing the initial cost savings, but
11 there is no plan yet to begin deployment?

12 THE WITNESS: It is in the development
13 stage. Based on the equipment that exists we
14 anticipate that there may be an opportunity, if
15 funding is approved with the limited capital that is
16 available and estimated, that maybe as many as 180
17 small parcel and bundle sorters that are converted.

18 CHAIRMAN GOLDWAY: The July 27, 2010,
19 technical conference response that you provided said
20 this project was in the planning stage. So are you
21 saying it is not in the planning stage?

22 THE WITNESS: It is in the planning stage of
23 determining the extent of the opportunity and the
24 investment and the extent of the deployment.

25 CHAIRMAN GOLDWAY: So you don't have any

1 information on what the projected savings will be yet
2 for 2011?

3 THE WITNESS: Not yet.

4 CHAIRMAN GOLDWAY: You don't have a
5 timeline?

6 THE WITNESS: No.

7 CHAIRMAN GOLDWAY: Maybe you could, because
8 this was a question among ourselves. Could you
9 clarify the different stages in this flat strategy
10 plan? What does planning mean? What does development
11 mean? There was a third stage as well.

12 We could not by the words themselves
13 determine what the differences were, and the word you
14 used in the report that you provided to us in July was
15 planning, and now you're saying the word is
16 development.

17 So could you help us to understand those
18 three different levels, three different stages of
19 projects?

20 THE WITNESS: The planning stage within our
21 Engineering function, the planning stage is where an
22 opportunity has been identified, the concept is
23 initiated, and the opportunities that the initiative
24 may afford are evaluated.

25 I would describe this initiative as being at

1 that stage. The concept of being tested within
2 Engineering and as a result of that initial testing,
3 developing the initiative for review and approval for
4 funding within the Postal Service.

5 CHAIRMAN GOLDWAY: So this concept is being
6 tested within Engineering at the moment?

7 THE WITNESS: That's how I would describe
8 it.

9 CHAIRMAN GOLDWAY: Okay. That's planning.
10 And then what's development?

11 THE WITNESS: Development would be the
12 initial testing, and if it's proven that this will be
13 an effective initiative we would likely test at a
14 number of locations, identifying the number of
15 locations that we would test the initiative, and
16 deploy an initial set of equipment for the testing of
17 the concept.

18 CHAIRMAN GOLDWAY: And what's the last
19 stage?

20 THE WITNESS: Once the decision is made for
21 deployment, deploying the equipment.

22 CHAIRMAN GOLDWAY: So we have planning,
23 development and deployment, right?

24 THE WITNESS: Yes.

25 CHAIRMAN GOLDWAY: The concept is before

1 planning, the concept stage? The concept is within
2 the planning stage?

3 THE WITNESS: I would describe it as within
4 the planning stage.

5 CHAIRMAN GOLDWAY: We had understood the
6 concept was sort of the beginning, but you're saying
7 the planning stage identifies opportunities and
8 concepts and then the concepts are tested and that's
9 all within the planning stage? Yes?

10 We're trying to clarify what's not very
11 clear to us. So we've got a planning stage, a
12 development stage and a deployment stage, and within
13 planning there's a concept stage. Is that the way you
14 want to say it now?

15 THE WITNESS: Well, initially an opportunity
16 is identified as a concept, and planning begins once
17 that concept, once that opportunity, is identified.

18 CHAIRMAN GOLDWAY: Okay. But you listed in
19 your report several things that were in the concept,
20 others that were in the planning stage, others that
21 were in the development stage. Now you're sort of
22 muddying concept and planning here so that we can't
23 really distinguish where they are.

24 I think I'll ask my staff to go back and
25 look at what you submitted and see if they can't get

1 you to clarify where some of those projects are that
2 you've identified as concepts and to maybe clarify
3 where they are in the planning stage.

4 COMMISSIONER LANGLEY: Madam Chairman, could
5 I just ask for a moment that we also add where the
6 cost savings associated with these proposals, at what
7 point they are assigned?

8 CHAIRMAN GOLDWAY: That's a good question,
9 but my understanding is -- well, you tell us. Where
10 are the cost savings?

11 COMMISSIONER LANGLEY: I mean, are there
12 discrete --

13 CHAIRMAN GOLDWAY: Right.

14 COMMISSIONER LANGLEY: -- cost savings
15 embedded in each of these steps? I don't want to take
16 away from the Chairman's time, but I think --

17 CHAIRMAN GOLDWAY: Yes.

18 COMMISSIONER LANGLEY: -- how all this is
19 melded together.

20 THE WITNESS: In the development of any
21 initiative, as that initiative is being pursued the
22 opportunities are identified for where there could be
23 work hour savings associated with whatever the
24 initiative is.

25 As the initiative progresses and we identify

1 those opportunities, those are developed into a
2 decision analysis for investment purposes, so once
3 that decision analysis is completed and we are all in
4 agreement on where the savings opportunities are the
5 funding is approved for the initiative.

6 CHAIRMAN GOLDWAY: So you wouldn't begin
7 what you've just called development, which is initial
8 testing, unless you had had a decision analysis that
9 showed that there were savings?

10 THE WITNESS: And if savings opportunities
11 are identified, there could also be testing on a
12 limited basis with limited funding prior to full
13 deployment or approval for funding for full
14 deployment.

15 COMMISSIONER LANGLEY: So a plan to
16 implement a plan doesn't come after the testing?

17 THE WITNESS: I'm sorry. A plan to
18 implement?

19 COMMISSIONER LANGLEY: When would a decision
20 be made to go full bore with a new program?

21 THE WITNESS: Once the decision analysis is
22 completed and presented to the funding committees
23 within the Postal Service for approval, senior
24 management approval, depending on the funding level
25 and the amount of the investment. Then once that

1 decision is made with the approval of the funding then
2 it would go forward.

3 COMMISSIONER LANGLEY: But you mentioned
4 limited funds could be released for limited testing?

5 THE WITNESS: Correct.

6 CHAIRMAN GOLDWAY: Do you have DARs for the
7 programs in development and in planning?

8 THE WITNESS: The program that you referred
9 to?

10 CHAIRMAN GOLDWAY: Yes.

11 THE WITNESS: We do not at this point have a
12 DAR completed for that program.

13 CHAIRMAN GOLDWAY: So there's no DAR for the
14 automated package and bundle sorter yet?

15 THE WITNESS: Not at this time.

16 CHAIRMAN GOLDWAY: Do you have a timeline
17 when you think you'll make a decision on them?

18 THE WITNESS: I could reach out to
19 Engineering and determine what that timeline is.

20 CHAIRMAN GOLDWAY: We'd appreciate that
21 information. Any other questions along this line?

22 (No response.)

23 CHAIRMAN GOLDWAY: Time-Warner has a
24 question that they wanted us to ask. What is the
25 standard operating procedure for processing periodical

1 flats with a manual incoming secondary sort when the
2 mailing arrived after the published critical entry
3 time?

4 THE WITNESS: Madam Chairman, we operate
5 within a processing window described within our
6 operating plans. Our operating plans define critical
7 entry times and clearance times for operations.

8 Our expectation is that the field process
9 mail in the most efficient manner and at their
10 discretion make a decision in what manner that mail is
11 processed. We expect and monitor performance to
12 ensure that the most efficient manner of processing is
13 being utilized.

14 It's our expectation that mail that arrives
15 prior to the critical entry time is processed within
16 the most efficient manner. We recognize that at the
17 local level decisions are made, and it's been
18 identified that decisions have been made at some
19 locations to work mail manually.

20 And where that is occurring, if it is
21 occurring for mail that's received after the critical
22 entry time, we are very interested in that information
23 as to where it may be occurring so that we could
24 encourage the correct decisions by local managers to
25 work that mail efficiency on automated processing

1 equipment, mechanized processing equipment, as opposed
2 to manually.

3 CHAIRMAN GOLDWAY: Well, what policies are
4 currently in effect to maximize the amount of
5 periodical mail processed on automated piece sorting
6 equipment when the mailing arrives after the
7 automation bundle sorting equipment has finished the
8 run for the day or to encourage the local operators,
9 the local processing center, to use automation
10 equipment at any time?

11 THE WITNESS: It's our expectation that mail
12 is processed on automated and mechanized equipment
13 where it is available and when it is available.
14 Ultimately the decision that local management --
15 decisions are at their discretion. If in fact they're
16 facing variables that may be impacting their
17 operations, other influences on their operations, that
18 may force them to make other decisions.

19 The discretion exists at the local level for
20 managers to make decisions, but overall we monitor the
21 performance of operations to drive the correct
22 behavior and to drive work on the most efficient
23 processing manner that is available.

24 CHAIRMAN GOLDWAY: Well, how do you monitor
25 it at the same time that you give full discretion to

1 the local decision maker?

2 THE WITNESS: There's indicators,
3 performance indicators that we monitor, utilization of
4 equipment, the workload that's worked, the processing
5 window analysis, the number of hours that the
6 equipment is processing mail, the windows of operation
7 compared to when the mail is available.

8 Typically within our processing facilities
9 there are planned windows of operation, and we compare
10 the actual windows of operation -- performance
11 indicators such as throughput, run hours -- to those
12 windows of operation to ensure that mail is being run
13 in the most efficient manner, but we have managers in
14 the field with the discretion to make decisions where
15 it's necessary.

16 CHAIRMAN GOLDWAY: What is the standard
17 operating procedure for processing standard mail flats
18 with a manual income secondary sort when the mailing
19 arrived after the published critical entry time?

20 THE WITNESS: If I understand the question
21 correctly, if the operation is a manual incoming
22 secondary then the standard operating procedure would
23 be to process that mail manually.

24 But if you're describing an operation that
25 has mechanized equipment the expectation is that if

1 that equipment, based on the schedule of that
2 equipment for the various operations that are
3 processed on that equipment, if that operation is
4 scheduled for that equipment that that mail be worked
5 on automated and mechanized equipment.

6 CHAIRMAN GOLDWAY: Do you process standard
7 mail bundles manually when they could be processed on
8 automation?

9 THE WITNESS: Our expectation is that our
10 field managers make the decision to process it on
11 automated and mechanized equipment and not process it
12 manually when it's available.

13 CHAIRMAN GOLDWAY: And what are the policies
14 currently in effect to maximize the amount of standard
15 mail flats processed on automation piece sorting
16 equipment when the mailing arrives after the
17 automation bundle sorting equipment has finished the
18 run for the day?

19 THE WITNESS: I would describe it as an
20 expectation, and as we identify performance results we
21 identify where there may be opportunities for the
22 field to improve their performance. If in fact they
23 are not taking full advantage of those opportunities
24 we provide that direction in identifying those
25 opportunities with the field.

1 The expectation is they are in the field.
2 What I'm trying to describe is an environment where
3 the expectation is there to work the mail in the most
4 efficient manner possible.

5 If the equipment is available, the
6 expectation is there that mail is worked on the
7 equipment. Are there instances where that might not
8 be happening? Yes, and we address those issues when
9 we identify them.

10 CHAIRMAN GOLDWAY: Can you say affirmatively
11 that this manual processing is happening less
12 frequently than it has happened in the past?

13 THE WITNESS: I can't say that there is a
14 great deal of attention on the utilization of our
15 equipment and that we are driving behavior to in fact
16 utilize that equipment to the maximum extent possible.

17 CHAIRMAN GOLDWAY: This is a Hot 2C
18 question. Has the Postal Service performed any
19 studies concerning the extent and cost of manual
20 bundle and piece processing of automation compatible
21 mail, especially in regard to Hot 2C and Hot 3C
22 procedures?

23 THE WITNESS: No specific study that I'm
24 aware of.

25 CHAIRMAN GOLDWAY: Are you aware of the

1 conclusion in the recent OIG report, EAAR10-007, that
2 the FSS may not be a profitable venture for the Postal
3 Service?

4 THE WITNESS: I am aware that the report was
5 issued recently, but I have not reviewed the report,
6 no.

7 CHAIRMAN GOLDWAY: The report indicates that
8 the return on investment will not be able to be
9 captured. There will be not enough savings, if
10 savings at all, from the FSS machines.

11 Has the AFSM been successful at reducing
12 flat processing costs? Enough to make flats
13 processing profitable?

14 THE WITNESS: I can't speak to the
15 profitability, but I can say that the AFSM introduced
16 an improved level of productivity to the operations.

17 CHAIRMAN GOLDWAY: Do you have a measurement
18 of what that improved productivity is?

19 THE WITNESS: Prior to the AFSM-100s when we
20 had flat sorter 881s, the throughput was approximately
21 5,500 pieces per hour at a per activity rate of 919
22 pieces. With the AFSM-100, our throughput is
23 approximately 13,800 with a productivity rate of
24 approximately 1,700 pieces per hour.

25 CHAIRMAN GOLDWAY: We don't know whether

1 that increase in profitability, however, is enough to
2 eliminate the below water impact of the flats?

3 THE WITNESS: I cannot speak to that.

4 CHAIRMAN GOLDWAY: This next question refers
5 to the honest, efficient, economical management
6 requirements of the PAEA for the Postal Service. When
7 did the Postal Service begin to lose money on standard
8 mail noncarrier route flats?

9 THE WITNESS: Madam Chairman, respectfully
10 my knowledge is in Operations, and I cannot answer
11 questions related to --

12 CHAIRMAN GOLDWAY: How long have you worked
13 in Operations, which included flats? How many years?

14 THE WITNESS: Madam Chairman, I've worked in
15 Operations in the Postal Service my entire career, for
16 26 years.

17 CHAIRMAN GOLDWAY: Was there any expression
18 ever given to you by other people on your team or
19 above you that said we have a problem with standard
20 mail noncarrier route flats?

21 THE WITNESS: My knowledge and the extent of
22 my responsibility includes identifying the
23 opportunities to operate more efficiently and
24 identifying the opportunities for reducing work hours.

25 That is my responsibilities within the

1 Postal Service and driving the policies within
2 Operations to --

3 CHAIRMAN GOLDWAY: I take it you were given
4 some direction to specifically pay attention to flats,
5 standards flats, at some time, at some point in your
6 career? After all, you're here representing --

7 THE WITNESS: Yes.

8 CHAIRMAN GOLDWAY: -- the flat strategy. Do
9 you have a date when that occurred?

10 THE WITNESS: Well, in my various roles in
11 the Postal Service as an operations manager, as a
12 plant manager -- I was a plant manager in three
13 various locations -- in the field, in that role I
14 managed operations so that we can operate efficiently
15 and improve our performance.

16 In my role here at Headquarters I drive
17 policies in the field and I develop policies for the
18 field that are related to operating efficiently.

19 CHAIRMAN GOLDWAY: Are you aware that
20 standard mail and periodicals --

21 THE WITNESS: Yes, I am.

22 CHAIRMAN GOLDWAY: When did you become aware
23 of that?

24 THE WITNESS: I've been aware for many years
25 that that's been the case.

1 CHAIRMAN GOLDWAY: How many? Five? Ten?

2 THE WITNESS: Ten.

3 CHAIRMAN GOLDWAY: Ten. Ten years. And
4 that's for both periodicals and flats?

5 THE WITNESS: I am aware, yes.

6 CHAIRMAN GOLDWAY: And do you know when the
7 AFSM rollout was completed?

8 THE WITNESS: Madam Chairman, I believe it
9 was in 2002.

10 CHAIRMAN GOLDWAY: 2002.

11 THE WITNESS: I would have to verify that
12 information.

13 CHAIRMAN GOLDWAY: And does the document,
14 Flat Strategy, contain the Postal Service's plan to
15 improve the cost coverage of standard flats and
16 periodicals?

17 THE WITNESS: The document, Flat Strategy,
18 was intended to improve efficiencies and reduce costs.

19 CHAIRMAN GOLDWAY: There's no relationship
20 of the cost reduction to the actual cost of flats and
21 periodicals to be sure that the cost reductions end up
22 by providing some measure of profitability for those
23 two products?

24 THE WITNESS: I believe the opportunities
25 for reducing work hours is the relationship.

1 CHAIRMAN GOLDWAY: But there's no
2 documentation that defines the number of work hours
3 that are going to be reduced and relates it to
4 specific numbers of cost savings so that periodicals
5 and flats would in fact cover their costs?

6 THE WITNESS: Not that I'm aware of.

7 CHAIRMAN GOLDWAY: Nothing in the plan that
8 does that?

9 THE WITNESS: Not in the flat strategy.

10 CHAIRMAN GOLDWAY: How many of the programs
11 have planned implementation dates in the flat
12 strategy?

13 (Pause.)

14 THE WITNESS: Quickly going through this,
15 Madam Chairman, and I would like the opportunity to
16 provide a more accurate answer. I would say four or
17 five of these programs have implementation dates or
18 implementation plans.

19 CHAIRMAN GOLDWAY: Only four or five have.
20 And when you go back over that and report to us, could
21 you give us the planned implementation dates? How
22 many of these programs will require a DAR before
23 implementation?

24 THE WITNESS: I would have to provide that
25 information.

1 CHAIRMAN GOLDWAY: And how many programs
2 currently have a DAR, and how many of the programs
3 having DARs are in the development stage?

4 Why do you think these clearly largely
5 hypothetical strategies that you've listed in this
6 document will lead to cost reductions for flats where
7 other programs in the past have failed?

8 THE WITNESS: I believe just as other
9 programs, any initiative starts with a concept and
10 starts with an idea. We begin planning and developing
11 that idea, and I don't know whether or not any of
12 these programs will lead to savings.

13 The development of those ideas will answer
14 that question. The development of the DARs will
15 answer that question.

16 CHAIRMAN GOLDWAY: Has the Postal Service
17 learned anything in the attempts thus far with regard
18 to AFSM or other projects that it could use in the
19 future where it's failed? Has it learned anything
20 from where it's failed that it could apply to the
21 future?

22 THE WITNESS: I believe that we, as any
23 organization, do learn from our experiences. I'm not
24 sure that I would describe any of our initiatives
25 specifically from a general description as having

1 failed, but I will state that we do learn from our
2 experiences and build on those experiences for future
3 opportunities as we develop them.

4 COMMISSIONER ACTON: Mr. Neri, could you
5 talk a bit about what you regard the measure of
6 failure or success? What's the goal when you're
7 testing or implementing these concepts or plans?

8 THE WITNESS: My description of failure or
9 success is whether or not the initiative proves true
10 to the expectations, whether or not the savings
11 opportunities that were identified with that
12 initiative are achieved.

13 COMMISSIONER ACTON: Okay. That's key
14 because you know, of course, that it's a compliance
15 issue for the regulator covering these costs. That's
16 our driver for our interest in this concern.

17 So if you understand that the plan you're
18 conceiving and developing and implementing is in the
19 end supposed to achieve a goal which will cover those
20 cost gaps then that's what we're looking for.

21 CHAIRMAN GOLDWAY: It doesn't appear that
22 you've got any direct relationship, though, between
23 your plans and actual cost savings.

24 This document that you prepared that's in
25 response to the PRC's directive is providing a

1 description of the strategies the Postal Service has
2 implemented and intends to implement in the future to
3 address these issues.

4 But if this isn't a strategy to improve cost
5 coverage, just a general idea of what will gain some
6 general efficiencies, where is that strategy?

7 THE WITNESS: Madam Chairman, these are
8 strategies that we are pursuing in order to identify
9 where we can reduce costs.

10 COMMISSIONER ACTON: Mr. Neri? I'm sorry,
11 Madam Chair.

12 CHAIRMAN GOLDWAY: Go ahead. Go ahead.

13 COMMISSIONER ACTON: Mr. Neri, can you
14 outline for me the new programs that have been
15 developed for flat processing during the past 12
16 months? Which are those?

17 THE WITNESS: FSS is one that is in the
18 deployment stage. We are deploying equipment for flat
19 sequenced sorting. That's one program.

20 And along with that is the integration of
21 that operation within our processing facilities, so
22 there's been a great deal of resources focused on the
23 success integration of the flat sequencers within our
24 operations.

25 COMMISSIONER ACTON: Okay. And I think the

1 Chairman referenced earlier a report by the Office of
2 Inspector General to the Postal Service that addresses
3 some of his concerns about the FSS.

4 I would encourage you to review it because
5 it may provide you some guidance on how to target some
6 of your resource since I believe you indicated that
7 you're not familiar with those findings.

8 CHAIRMAN GOLDWAY: If your strategy was
9 meant to improve cost coverage and you are not
10 familiar with the way the OIG has evaluated cost
11 coverage I think you'd better review that document to
12 be informed of how cost coverage is evaluated for
13 efficiencies.

14 In the AFSM, for instance, or any of the
15 other implemented changes from stacks to bundles or
16 co-palletization, et cetera, have you found any
17 unintended consequences of your efficiencies that have
18 resulted in additional cost?

19 THE WITNESS: I'm sorry. With regard to the
20 AFSM?

21 CHAIRMAN GOLDWAY: Over the years with the
22 AFSM or with any of the other strategies or procedures
23 that have been implemented in the last 10 years to
24 deal with flats to try to make them more efficient,
25 have you discovered any unintended consequences that

1 have raised costs?

2 I've been on the Commission for 12 years,
3 and for 12 years I've heard about projects that are
4 going to save costs within flat handling. If you add
5 up all of those projects and ideas, one would think
6 that flats would cost zero because of all of those
7 brilliant ideas, and yet we're still here with costs
8 even greater than what the prices are that we can
9 charge for periodicals.

10 The difference between the cost and the
11 coverage is expanding all the time, so there must be
12 some problems in the last 10 or 12 years. Have you
13 identified any of those problems?

14 THE WITNESS: In answer to your question,
15 Madam Chairman, I am not aware of any unintended
16 consequences for any particular program.

17 CHAIRMAN GOLDWAY: And you're not aware of
18 any areas that have developed in the last 10 years
19 that increased costs for periodicals?

20 THE WITNESS: No, I am not.

21 CHAIRMAN GOLDWAY: Well, this is a
22 frustrating exercise. I will ask my other Commission
23 colleagues if they'd like to take a stab at this.
24 Commissioner Blair?

25 COMMISSIONER BLAIR: Thank you, and I

1 apologize for coming in late. The storms this morning
2 blocked my access, so I appreciate your patience with
3 me.

4 I think the discussion we're having right
5 now about flats and the frustration of the Commission
6 reflects the frustration in the community. It's all
7 about how to bring these costs down.

8 One thing I wanted to ask you just as more
9 of a big picture question is that it seemed to me in
10 reviewing the Postal Service's submission this time
11 that with the rates that were proposed it seemed to be
12 moving closer to covering costs for those products
13 that were currently under water.

14 I want to know what kind of priority is it
15 for the Postal Service, or is it a priority, that
16 rates cover costs under this new PAEA environment? Is
17 it a priority for the Postal Service to have prices
18 that cover rates, that cover costs?

19 THE WITNESS: Commissioner, I would not be
20 the best individual from the Postal Service to answer
21 that question with my operational responsibilities,
22 not pricing responsibilities, so I'm not in a position
23 to be able to answer that question.

24 CHAIRMAN GOLDWAY: You're not given any
25 targets in your operations to say okay, we need to

1 save this amount of money in order to --

2 THE WITNESS: Yes, Madam Chairman.

3 CHAIRMAN GOLDWAY: -- make this product
4 profitable?

5 THE WITNESS: In fact, Madam Chairman, I am
6 given targets, performance targets for budgets,
7 achieving our budget. Operations has a budget that
8 are issued, and we develop strategies and initiatives
9 within Operations in order to achieve our budget.

10 COMMISSIONER BLAIR: Do those budgets have a
11 relationship to the prices that are charged? If so,
12 what is that relationship?

13 THE WITNESS: Our budgets have a
14 relationship to the revenue that the Postal Service
15 generates.

16 COMMISSIONER BLAIR: What's that
17 relationship? Is it one-for-one? I'm just trying to
18 get a better sense of how budgets -- you said that you
19 can't answer the initial question, but you're involved
20 in the operations.

21 I think it would be interesting to better
22 know how the budgets that you receive are related to
23 the revenues that the Postal Service is bringing in.

24 THE WITNESS: Respectfully, I believe that
25 that would be a better question for Finance.

1 CHAIRMAN GOLDWAY: Are you asked to meet a
2 certain budget by product? In other words, what I'm
3 imagining is that you have to demonstrate that you
4 provided a certain amount of total savings.

5 THE WITNESS: Yes.

6 CHAIRMAN GOLDWAY: Do you have to do that by
7 product?

8 THE WITNESS: We have to accomplish budget
9 performance, and we monitor performance by operation
10 so we set expectations for individual operations
11 within the capabilities of those individual
12 operations.

13 CHAIRMAN GOLDWAY: So the operations would
14 be what?

15 THE WITNESS: Letter processing, flat
16 processing. So individual operations have performance
17 measures, and the results of those individual
18 operations are collectively measured and bottom line
19 assessed as to whether or not we're achieving the
20 budget.

21 CHAIRMAN GOLDWAY: But not by product?

22 THE WITNESS: Not within Operations, no.

23 CHAIRMAN GOLDWAY: How has the flats
24 processing operation been performing in relationship
25 to its budget?

1 THE WITNESS: I would have to provide that
2 detailed information.

3 CHAIRMAN GOLDWAY: Could you do that for us?

4 THE WITNESS: Yes.

5 CHAIRMAN GOLDWAY: Thank you.

6 COMMISSIONER LANGLEY: At what point would
7 the flats processing performance in relation to its
8 budget be integrated with other parts of the operation
9 so that there is this review of meeting performance
10 levels?

11 THE WITNESS: For our individual operations
12 we have performance indicators for activity
13 performance, and those are established.

14 Targets are established, and based on the
15 performance compared to those targets the
16 opportunities are identified where in fact we set
17 expectations for improved performance from the field,
18 from field managers.

19 COMMISSIONER LANGLEY: And then how are the
20 times that there is manual processing of flats rather
21 than going through automation? How is that brought
22 in? How is that factored in, if at all?

23 THE WITNESS: We do evaluate the utilization
24 of equipment and drive behavior to improve that
25 utilization if the opportunity exists.

1 In fact, there is work being performed
2 manually during the same processing windows that may
3 reflect an opportunity of capacity that exists on
4 equipment. Then the expectation is that that capacity
5 is utilized and the mail is processed in the most
6 efficient manner possible on the mechanized and
7 automated equipment.

8 COMMISSIONER LANGLEY: Is there any weight
9 given to meeting the target?

10 THE WITNESS: Absolutely. Within our
11 operating plans we balance our cost initiatives with
12 meeting service expectations.

13 COMMISSIONER LANGLEY: Thank you. Sorry,
14 Commissioner Blair.

15 COMMISSIONER BLAIR: That's okay. I think
16 that's an important point that you just brought out,
17 Commissioner Langley, that there are service standards
18 incorporated in there, but I'm still not seeing where
19 an overall budget strategy is involved in the
20 implementation or establishment of these expectations
21 from true performance. If performance isn't improved,
22 what happens? Do budgets increase? Decrease?

23 THE WITNESS: We do not reward poor
24 performance with lower expectations. No, we do not.
25 There's an accountability.

1 COMMISSIONER BLAIR: But it seems that your
2 intent has been frustrated over the past few years in
3 trying to make the FSS and the other flats processing
4 programs more efficient.

5 I'm trying to reconcile what I see as a
6 continuing frustration in not being able to achieve --
7 or are you achieving? I think Commissioner Acton
8 asked this question. Are you meeting expectations
9 with your flats processing?

10 THE WITNESS: I would have to review some
11 indicators to answer that question, sir.

12 COMMISSIONER BLAIR: What would be those
13 indicators?

14 THE WITNESS: Productivity, performance.

15 COMMISSIONER BLAIR: If you could provide
16 that for us, I think that would be helpful as we go
17 down this difficult path.

18 CHAIRMAN GOLDWAY: Is it possible that flats
19 are brought in, or periodicals let's say. Periodicals
20 are brought into a plant and the automation equipment
21 has been shut off for one reason or another and the
22 plant manager determines that given service standard
23 requirements and the small volume of periodicals that
24 are presented to him that for that particular instance
25 it's just simpler to sort them manually?

1 THE WITNESS: It's possible that that
2 occurs.

3 CHAIRMAN GOLDWAY: And will that plant
4 manager then be asked to justify why he's done that
5 for you, or will it just be part of the noise of the
6 report because overall his service performance is fine
7 and overall his cost reductions, hourly reductions,
8 are fine? How would you be able to track that
9 decision?

10 THE WITNESS: Madam Chairman, we have
11 specifically identified that in fact there are
12 instances and there are locations where what you've
13 described does occur, mail arriving after the critical
14 entry time and being worked less efficiently.

15 We are communicating -- monitoring and
16 communicating -- that that in fact is not an
17 expectation that we hold within our responsibilities.
18 You know, my responsibility is to drive the
19 expectations. That is not a behavior that we support,
20 and we in fact are addressing that and recognizing
21 that it does occur out there in the field.

22 CHAIRMAN GOLDWAY: Have you ever given any
23 thought to the fact that you invested all this money
24 and are investing even more in these highly automated
25 machines but that the volume flows are such that it

1 may not be worth the investment?

2 That seems to be what the OIG is saying;
3 that you might be better off figuring out some other
4 low tech ways to deal with this. Has that ever
5 crossed your mind since there doesn't seem to be
6 enough volume in the FSS at the moment to justify its
7 investment? The throughput isn't as fast as you
8 expected it to be, and there's not enough volume even
9 if the throughput were faster.

10 THE WITNESS: To generally answer your
11 question, I would state that we consider all
12 opportunities when considering how we can improve the
13 efficiency of our operations.

14 Specifically for the FSS, again I can't
15 comment on the OIG report and their findings and
16 whether or not we're in agreement with those findings.
17 At this time I can't answer to that. The report was
18 not directed to me, but I will become familiar with
19 the report.

20 With regard to the drop in volume which you
21 described, we are redeploying and have modified our
22 deployment plans for the FSS by redirecting a number
23 of machines to additional sites to expand the coverage
24 because of the drop in volume in the original sites
25 that they were scheduled to be deployed to.

1 Originally the 100 machines which are in the
2 process of being deployed were scheduled for 34
3 locations. That's now been increased to 47 locations,
4 so the same 100 machines will now be spread to 47
5 locations, providing the opportunity for deeper
6 penetration in more locations so that the lost
7 opportunity from the top in volume from the original
8 locations will now be replaced by being able to expand
9 it to additional zones and carrier routes to be
10 processed on the FSS.

11 CHAIRMAN GOLDWAY: You didn't think about
12 perhaps not taking all 100 machines?

13 THE WITNESS: It's a contractual issue with
14 the investment which was made.

15 CHAIRMAN GOLDWAY: Do you know if in plants
16 currently there are bundles that are being processed
17 manually even if the automation bundle sorter
18 equipment is running? What would make a plant manager
19 choose to do that?

20 THE WITNESS: Well, one situation may be if
21 it is running what operation is running on that
22 equipment. Is the operation the same operation that
23 may be performed manually simultaneous?

24 Again, operations. There are prescribed,
25 defined processing windows for each operation in order

1 to meet the expectations of the network, the dispatch
2 schedules for the network, and if there is an
3 operation scheduled on the equipment there may be
4 other operations that are performed simultaneous to
5 that operation so that those dispatches can be met in
6 order to meet service standards.

7 Now, that doesn't eliminate the possibility
8 that there may be the wrong decision being made out
9 there or the wrong behavior out there and mail could
10 be worked manually. If that's identified, it's
11 addressed.

12 VICE CHAIRMAN HAMMOND: Madam Chairman,
13 along with your line of questioning could I ask a
14 question right now?

15 CHAIRMAN GOLDWAY: By all means. That's
16 where we're here for.

17 VICE CHAIRMAN HAMMOND: Okay. Mr. Neri,
18 you've been discussing with the Chairman especially on
19 this question of manual processing instead of
20 automation, being on automation equipment, and you
21 talk about the most efficient processing way.

22 You leave that up to the local plant manager
23 is basically what I understand your answer to the
24 Chairman is. I've heard this discussed before that
25 that's what the Postal Service does is leave it up to

1 the local plant manager, who is supposed to follow the
2 most efficient processing. That's essentially what
3 you've said, isn't it?

4 THE WITNESS: The expectation is that the
5 most efficient processes are utilized within the
6 operations, and the plant manager is making those
7 decisions that result in the performance levels that
8 we expect, but in fact local managers have the
9 discretion to make the decision when necessary.

10 VICE CHAIRMAN HAMMOND: Okay. So would you
11 say when you find that they're not following this most
12 efficient processing way generally it's when they're
13 manually processing mail that ought to be automated
14 more likely than not from my understanding, but you
15 say you deal with it when it comes to your attention.

16 I was wondering. Well, how do you deal with
17 it? I mean, what's the penalty for getting caught? I
18 mean, is there training to correct it, or is there a
19 memo to file? I mean, you say you deal with it. What
20 do you do to correct the problem?

21 THE WITNESS: Commissioner, it's not my
22 intent to portray an environment that we don't have
23 efficient processes out there or managers making the
24 correct decisions.

25 In fact, the performance level that our

1 managers out there are achieving are exceptional. We
2 continue to improve productivities across the country.
3 We continue to operate with fewer employees and match
4 our work hours, reduce our work hours to the workload
5 reductions that we've been experiencing since 2006.

6 I described that since 2006 the Postal
7 Service is operating with about 111,000 fewer
8 employees, so we are driving efficiencies and our
9 managers are performing.

10 I was asked specific questions about whether
11 or not these instances occur. They do occur. I
12 believe they occur on a very limited basis. Some have
13 been behavior that have occurred over years in
14 managers and supervisors within Operations believing
15 that they were doing the right thing for service in
16 working this mail within the processing windows, mail
17 that arrives late.

18 We are educating our managers in fact that
19 we have operating plans to meet. We want to process
20 all the mail in the most efficient manner and that in
21 fact the mail that arrives after critical entry times
22 we are still meeting service expectations by holding
23 that mail to work on the automated systems, so it's a
24 matter of educating and it's a matter of changing
25 behavior that may occur in some isolated locations.

1 VICE CHAIRMAN HAMMOND: So you don't really
2 have a problem?

3 CHAIRMAN GOLDWAY: Well, we got an answer to
4 an interrogatory that said that 30 percent of mail is
5 handled manually.

6 VICE CHAIRMAN HAMMOND: Yes, but that's not
7 being incorrectly handled. There's no problem with
8 that.

9 I mean, I do hear once again that when you
10 talk about mail arriving late, et cetera, et cetera,
11 it's usually the mailer's fault. It's not anyone at
12 the U.S. Postal Service's fault. It's usually the
13 mailer's fault. Is that correct?

14 THE WITNESS: Commissioner and Madam
15 Chairman, the statement about 30 percent of the mail
16 being worked manually, without knowing the specifics
17 of that interrogatory I do believe that it includes
18 our manual operations at every post office across the
19 country so it's not the manual percentages.

20 It's not the manual workload or mail that's
21 being worked manually within our processing centers.
22 I believe that that's all of the processes and
23 accumulated percentage of all of the processes not
24 only in processing center facilities, but also local
25 post offices.

1 VICE CHAIRMAN HAMMOND: So back to my
2 original question on this. Are you saying that it is
3 the fault of the mailer or the Postal Service?

4 THE WITNESS: I don't believe it's anyone's
5 fault. I believe that it's the result of a practice
6 that has been occurring over the years, and I believe
7 that requires both a re-education of -- a continuous
8 education of -- our employees, our managers and the
9 education of our mailers as well.

10 VICE CHAIRMAN HAMMOND: So it's not really
11 that big of a problem and when it does occur you
12 re-educate them. That's how you specifically deal
13 with it. Is that what you're saying?

14 THE WITNESS: I would say that's accurate.

15 VICE CHAIRMAN HAMMOND: Okay. Thank you.

16 CHAIRMAN GOLDWAY: But again, there's no
17 direction with regard to cost savings specifically
18 directed by product, so when you have a flat strategy
19 that you presented to us it doesn't include any
20 relationship between savings and cost coverage?

21 THE WITNESS: I believe I described it as
22 our initiatives identifying cost savings by operation,
23 and that would be the link to the product.

24 CHAIRMAN GOLDWAY: To the extent it's linked
25 to a product.

1 COMMISSIONER BLAIR: Madam Chair?

2 CHAIRMAN GOLDWAY: I think I've gotten as
3 much information as I can, but if there are more
4 questions?

5 COMMISSIONER BLAIR: Just a followup on
6 this. I was looking at a GAO report that came out in
7 July of 2009, and the GAO report recognized that there
8 was progress being made with the FSS, but stated that
9 the future savings may be limited by the Postal
10 Service's lack of specific cost saving targets, which
11 we've been discussing up here, and results, which
12 again we've been discussing, for most of these
13 actions.

14 Without such information, the Postal Service
15 is unable to assess the contribution and performance
16 of each action and focus on those with the greatest
17 savings potentials. While we were encouraged by the
18 Postal Service's effort to coordinate with employees,
19 unions and mailers for more efficient delivery,
20 continued focus will be needed to help address ongoing
21 challenges related to declining volumes, technical
22 issues and financial and operational issues.

23 GAO recommended that cost saving targets and
24 tracking results for each of the major initiatives,
25 including FSS, be developed. Did you follow up on

1 those GAO recommendations?

2 THE WITNESS: Yes, Commissioner. In the
3 last year we have established targets for our FSS
4 operations, and we are monitoring those targets on a
5 continuous basis. We communicate through webinars and
6 teleconferences with our field managers at the
7 locations where that equipment has been deployed.

8 As we continue to deploy that equipment,
9 targets such as pieces sent, run time, throughput,
10 accept rates, DPS percentage for the flat sequence,
11 sir, have been put in place and are tracked and
12 reported on and are being utilized as indicators to
13 drive performance.

14 CHAIRMAN GOLDWAY: But they drive
15 performance of the machine. They don't drive
16 performance of the reduced cost of the product on the
17 machine. There seems to be a disconnect.

18 COMMISSIONER BLAIR: Right. I mean, are
19 they again tied to any kind of budget?

20 THE WITNESS: Well, they're tied to the
21 operating budget of our processing operations and the
22 performance of the machine and cost savings that the
23 machine is intended on achieving is, in my opinion,
24 how it's tied to the product.

25 Now, Finance would have to better answer the

1 specific ties there, but I drive operational
2 performance. I drive cost reduction initiatives in
3 order to reduce our costs.

4 CHAIRMAN GOLDWAY: It's not a cost reduction
5 initiative for the operation of the product.

6 COMMISSIONER BLAIR: We're getting just part
7 of the picture.

8 CHAIRMAN GOLDWAY: Yes, yes.

9 COMMISSIONER BLAIR: And that you are
10 unable, unwilling but unable to answer the fuller
11 broader picture that we're asking.

12 COMMISSIONER LANGLEY: But also, if there is
13 a disconnect and we're looking pretty much just at the
14 operation of the machine, how does the Postal Service
15 even develop incentives within its pricing structure
16 to incentivize action on the part of the mailer when
17 the focus is really the machine?

18 THE WITNESS: I believe the focus is also
19 with the mailer, and working with the mailer on they
20 introducing the product for processing on our
21 machines. We just issued an optional FSS prep
22 opportunity through the Federal Register notice, an
23 opportunity for mailers to make up their mail into
24 bundles and pallets through the sorts meet level for
25 the FFS machine which allows mailers to create larger

1 bundles and qualify for carrier route pricing, and be
2 able to make more pallets that qualify for that
3 pricing.

4 So, I do believe that we do have initiatives
5 that provide those opportunities for the mailers, and
6 that's one example.

7 COMMISSIONER LANGLEY: But if we're looking
8 at problems and fully utilizing even the AFSM, and
9 we're not on the FFS, I think what my colleagues have
10 said is there needs to be more of a retrenchment maybe
11 so that you're looking at a much broader picture than
12 just the operation of the machines.

13 THE WITNESS: And our initiatives include
14 looking at opportunities such as that. AFSM
15 utilization is an area that we are currently analyzing
16 based on volumes of funds are our current locations
17 the best locations for all of our equipment. We are
18 evaluating the opportunity for redeploying equipment
19 from one location to another in order to increase our
20 utilization of that equipment.

21 Examples are sites that may have multiple
22 pieces of equipment, that we reduce the number at one
23 site and introduce the equipment at new sites in order
24 to have that coverage. So we are in fact looking at
25 those opportunities to increase utilization.

1 COMMISSIONER LANGLEY: Okay, I appreciate
2 that response. That actually helps me go into a
3 question that I have that is very non-contiguous state
4 and territory-related.

5 In a response to POIR-3, question 23,
6 regarding the L009, or L009, these are mixed states'
7 consolidation centers for mixed ADC flats. In the
8 flat strategy it's mentioned that the numbers would be
9 reduced from 40 sites to 18, and my understanding is
10 there is a site in Honolulu as well as Anchorage,
11 Alaska.

12 Are there sites in the Virgin Islands and
13 Puerto Rico as well?

14 THE WITNESS: Yes. Yes, Commissioner.

15 COMMISSIONER LANGLEY: Will these sites
16 continue to have an L009, will they continue to be
17 L009 processing sites after consolidation is completed
18 if it were approved?

19 THE WITNESS: Yes, they will.

20 COMMISSIONER LANGLEY: Okay, and will that
21 impact the consolidation on the U.S. mainland? Will
22 the consolidation on the U.S. mainland impact delivery
23 to Hawaii and other non-contiguous areas if there is a
24 consolidation?

25 THE WITNESS: The consolidation would have

1 no service impact.

2 COMMISSIONER LANGLEY: So there would be no
3 service impact --

4 THE WITNESS: Right.

5 COMMISSIONER LANGLEY: -- that the
6 residents --

7 THE WITNESS: Resulting from the
8 consolidation, correct.

9 COMMISSIONER LANGLEY: And at what stage is
10 it? Is there a DAR on this?

11 THE WITNESS: There is no DAR with this
12 initiative. This initiative is relocating operations
13 in consolidated locations, and we are -- within the
14 initiative we have established it at 15 locations of
15 the 18.

16 COMMISSIONER LANGLEY: Thank you very much.

17 COMMISSIONER ACTON: Mr. Neri, from some of
18 your discussion it seems like you're dealing with a
19 couple of important competing priorities. One would
20 be delivering the mail in a good and timely fashion
21 that meets service measure requirements, and the other
22 is trying to cut cost, and sometimes that may be at
23 odds. Is that a fair characterization of part of your
24 challenge?

25 THE WITNESS: I would describe it as -- that

1 in fact over time that's been a challenge, and that we
2 are developing more definitive lines within our
3 operating environment with critical entry times in our
4 operating plans and sharing those critical entry time
5 with mailers so that they have an expectation what is
6 the time that they must have the mail within our
7 operations, arriving at our operations so that we can
8 in fact meet those operating plans, and in fact meet
9 those service standards.

10 So, I believe that we are evolving and we
11 are educating both internally and externally so that
12 those guidelines provide us an opportunity to achieve
13 both.

14 COMMISSIONER ACTON: Okay. From what I can
15 glean from it, it seems as if you are trying to
16 implement some needed standardization of operations
17 and that part of the problem is that when you have
18 your local managers working to deliver mail in a
19 timely way, and occasionally they may be choosing to
20 deviate from some of those standard operations that
21 are designed to lower cost, and instead they are doing
22 what they need to do to move the mail in an
23 expeditious fashion. Am I grasping that properly?

24 THE WITNESS: There are times where that may
25 occur.

1 CHAIRMAN GOLDWAY: You know, I think the
2 point is that it may be for the individual plant that
3 the handling of the mail manually turns out for the
4 plant's operation to be more cost effective for the
5 plant because of the volumes and the various things
6 that are on the machine that are running that may not
7 be compatible with what comes in, and I think there is
8 a contradiction between the needs of the machine and
9 the needs of the plant in terms of where the cost
10 savings are, and I don't think that we have gotten the
11 nexus to solve that problem.

12 That seems to me as I have been watching
13 this problem with standard flats develop over the last
14 12 years that we haven't -- we haven't quite gotten to
15 what the real problem is.

16 COMMISSIONER ACTON: I suppose, Mr. Neri, I
17 just would like to leave you with the impression that
18 the reason we have so many questions about this is
19 that we rarely -- we very rarely have an opportunity
20 to have this kind of a candid exchange with someone
21 who is as close to what's happening as this. So we
22 have a lot of interest in knowing how the Postal
23 Service is managing the regulatory priorities of
24 meeting service measures which we've helped or had a
25 role in establishing as well as the compliance

1 concerns that we have expressed in our annual
2 determinations with respect to these cost coverages.
3 So we appreciate your input.

4 I have one last question, and that is, your
5 flat strategy document indicate that a Lean 6 Sigma
6 value stream map for periodicals is going to be
7 complete by August of this year. Is that accurate and
8 this is on schedule?

9 THE WITNESS: Yes, sir. We expect by the
10 end of this month to have the periodical process
11 within the Postal Service mapped, value stream map
12 from end to end, and if I could describe that it
13 identifies all of the steps of the process, and then
14 presents us the opportunity to identify projects that
15 we could launch for leaving out activities or steps of
16 that process.

17 COMMISSIONER ACTON: So you anticipate that
18 that steam map will be developed and available on
19 schedule later this year, and that it will likely
20 provide you some hopefully helpful insight on how to
21 target these concerns more effectively?

22 THE WITNESS: Yes.

23 COMMISSIONER ACTON: Thank you.

24 CHAIRMAN GOLDWAY: But there is no actual
25 cost saving target with the Lean 6 sigma, no dollar

1 amount, is there, or are there?

2 THE WITNESS: I'm sorry, Madam Chairman.

3 CHAIRMAN GOLDWAY: Are there --

4 THE WITNESS: The initiative which I
5 described is the first step to identifying
6 opportunities. It's mapping out the process from end
7 to end so that then projects could be developed for
8 leaving out steps of the process.

9 CHAIRMAN GOLDWAY: And the projects would go
10 through the same development stages, these three
11 development stages that you described earlier?

12 THE WITNESS: No, it's a different process.
13 It's a Lean 6 Sigma process which follows a prescribed
14 process of steps. It's called the Domaic process
15 where you define the problem. Once the process is
16 mapped from end to end, and following the steps you
17 define a potential problem that you want to solve.
18 Then you measure by collecting data on that process,
19 you analyze the data, you determine and implement
20 improvements, and then you put the controls in place
21 to sustain those improvements.

22 COMMISSIONER ACTON: I think it's well
23 established that the 6 Sigma approach is a very proven
24 tool for doing what you're outlining, and we have a
25 great interest in what you're trying to achieve, so

1 I'm hopeful that you will keep in mind that down the
2 road we'd like to learn more about this, and in fact
3 sometime after October 4th we will plan to remind the
4 Chairman that we might ask the senior management to
5 come and brief us on how that is progressing.

6 CHAIRMAN GOLDWAY: And it may well be that
7 that should be something that's submitted in the
8 annual report to meet our annual compliance
9 determination.

10 COMMISSIONER LANGLEY: May I ask Mr. Neri on
11 this Lean 6 Sigma initiative that you're undertaking
12 now?

13 At what point, if at all, are field
14 personnel brought into the discussion?

15 THE WITNESS: Commissioner, we have field
16 personnel involved today with the -- and mapping the
17 process having input. At this time I would estimate
18 about 20 individuals across the country at various
19 locations spread randomly around the country that have
20 input into effort, and as we identify opportunities
21 for projects we will also include field individuals on
22 those project teams.

23 COMMISSIONER LANGLEY: So are these 20
24 people managers, operations managers or are they at a
25 different level?

1 THE WITNESS: Support staff, operation
2 specialists, supervisors within operations.

3 COMMISSIONER LANGLEY: So some of them are
4 actually within plants?

5 THE WITNESS: Yes, most of them are within
6 plants.

7 COMMISSIONER LANGLEY: So their
8 understanding of whether things are going through an
9 automated process or manual processing is --

10 THE WITNESS: Correct.

11 COMMISSIONER LANGLEY: They are well versed
12 in that?

13 THE WITNESS: Correct.

14 COMMISSIONER LANGLEY: Thank you.

15 CHAIRMAN GOLDWAY: Vice Chairman Hammond.

16 VICE CHAIRMAN HAMMOND: Thank you. I had
17 just one more question.

18 Mr. Neri, have you ever designed on your own
19 or been asked to design by others at the Postal
20 Service under the managerial processing operation, a
21 very difficulty position, I understand?

22 When you have worked on such things have you
23 ever been asked to come up with anything in
24 consideration of a class or subclass of mail that
25 could end up driving that mail out of the system

1 because the Postal Service consider it unprofitable,
2 and it would be much better if the mail were to -- if
3 that type of mail was simply gone? Have you ever done
4 anything toward that end?

5 THE WITNESS: No, sir.

6 VICE CHAIRMAN HAMMOND: Okay, thank you.

7 CHAIRMAN GOLDWAY: I think that concludes
8 the questioning that we have for Witness Neri. There
9 is nothing further so I would like to reiterate my
10 fellow Commissioners' comments of appreciating your
11 testimony here today, and giving you the good news
12 that you are excused. Thank you very much.

13 THE WITNESS: Thank you.

14 (Witness excused.)

15 CHAIRMAN GOLDWAY: What I would like to do
16 is take a 10-minute break before we begin with our
17 next witness, and before I do that I did want to
18 acknowledge a couple of special guests who are in our
19 audience today. We are pleased and honored to have
20 with us today two guests from the National Postal
21 Agency of Ecuador, which is the postal regulator for
22 that country. Dr. William Said Reich, and Dr. Byron
23 Manchilauro. I'm not sure. I'm not pronouncing it,
24 Manchilauro, Deputy Director, Executive Director and
25 Deputy Director. Dr. Said and Dr. Lauro are visiting

1 the Commission for three days this week to learn more
2 about the role of our Commission and the U.S. Postal
3 System. They represent a regulator that is only two
4 years old, and one of the only independent postal
5 regulators in Latin America. Please join me in
6 welcoming them here today. They have been able to
7 witness our hearings firsthand and I hope they will be
8 able to stay for some more of the hearings later this
9 morning. Thank you very much for coming.

10 And with that we will reconvene at 11:10.

11 (Whereupon, a short recess was taken.)

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1 CHAIRMAN GOLDWAY: We will try and
2 reconvene. Before we begin with our witness, I'd like
3 to make a comment here. This inaugural Exigent Rate
4 case has required adaptability by all participants,
5 and this hearing is a prime example.

6 As I noted previously, we appreciate the
7 questions that parties have submitted in this
8 proceeding, and we intend to issue additional CHIRs as
9 the hearings conclude.

10 We also appreciate the Postal Service's
11 prompt responses to prior CHIRs, and the candor of
12 witnesses in responding to our questions.

13 Following yesterday's hearing, parties to
14 this proceeding filed pleadings requesting the
15 Commission to address two questions to the Postal
16 Service concerning statements made by witness Masse
17 during the hearing. The request, filed by the Parcel
18 Shippers Association, and jointly by the Alliance of
19 Nonprofit Mailers and the Magazine Publishers of
20 America, are in the nature of follow-ups and seek
21 clarification of witness Masse's statements.

22 One request seeks details of the projected
23 \$115 billion deficit for the period Fiscal 2009 to
24 Fiscal 2020. The other seeks data concerning the May
25 2009 price increase for non-flat machinable parcels.

1 The questions are reasonable. Accordingly,
2 the Postal Service is requested to provide responses
3 to the questions posed by the close of business day
4 August 13. Can you respond that that would be
5 acceptable? I believe you have the questions.

6 MR. RUBIN: Yes, the Postal Service should
7 be able to respond to those.

8 CHAIRMAN GOLDWAY: Thank you. Thank you for
9 being flexible and responsive.

10 Okay. Now we will proceed with our next
11 witness. Mr. Rubin, do you want to identify him?

12 MR. RUBIN: Thank you, Madame Chairman. The
13 Postal Service calls James M. Kiefer as its next
14 witness.

15 CHAIRMAN GOLDWAY: Mr. Kiefer.

16 Whereupon,

17 JAMES M. KIEFER

18 having been duly sworn, was called as a
19 witness herein and was examined and testified as
20 follows:

21 CHAIRMAN GOLDWAY: Thank you.

22 MR. RUBIN: We've provided Dr. Kiefer with
23 copies of a document titled, "Statement of James M.
24 Kiefer, On Behalf of the United States Postal
25 Service."

1 DIRECT EXAMINATION

2 BY MR. RUBIN:

3 Q Was this document prepared by you or under
4 your supervision?

5 A It was.

6 Q Does it contain the errata that were filed
7 on August 10, 2010?

8 A Yes, it does.

9 Q If you were to present this statement orally
10 here today, would this be your statement?

11 A Yes, it would.

12 Q There are also, associated with your
13 statement, five sets of pricing worksheets?

14 A Yes.

15 Q Are you prepared to sponsor those
16 worksheets?

17 A I am.

18 MR. RUBIN: So we will present the two
19 copies of your statement to the reporter, and we ask
20 that the statement and its associated worksheet be
21 entered into the record of this proceeding.

22 CHAIRMAN GOLDWAY: Thank you. Counsel,
23 please provide the reporter with two copies of the
24 statement of James M. Kiefer. The statement and its
25 associated library references are received into

1 evidence. However, as is our practice, it will not be
2 transcribed.

3 (The document referred to was
4 marked for identification and
5 was received in evidence.)

6 Dr. Kiefer has been identified as a Postal
7 Service representative prepared to attest to the
8 accuracy of answers to certain Presiding Officer
9 Information Requests; and, if necessary, to respond to
10 questions about those answers. A packet has been
11 prepared that includes Dr. Kiefer's answers.

12 Dr. Kiefer, can you confirm that the answers
13 contained in that packet are accurate, to the best of
14 your knowledge?

15 THE WITNESS: Yes, I can.

16 CHAIRMAN GOLDWAY: Counsel, will you please
17 provide the reporter with two copies of the answers of
18 Dr. Kiefer to Presiding Officer Information Request?

19 MR. RUBIN: Yes, we will.

20 CHAIRMAN GOLDWAY: His answers are received
21 into evidence, and are to be transcribed. And we're
22 now ready for questions from the Commission.

23 Dr. Kiefer, your statement covers a lot of
24 ground. And to help maintain an orderly record, the
25 Commission will start with some general questions, and

1 then it will take up questions related to each of the
2 classes and the proposed rates for each of those
3 classes.

4 We've already had some discussion with other
5 Postal Service representatives about how the size of
6 the requested increase was decided. Would you please
7 describe your role in determining the overall size of
8 the increase?

9 THE WITNESS: In this particular price
10 adjustment, as it was laid out in the Postal Service's
11 action plan issued in March, Postal Service management
12 determined that it would be appropriate to request a
13 moderate price increase, above CPI, so therefore
14 requiring the use of the exigent price change
15 mechanism.

16 And we were told that, in general, we were
17 asked to provide prices that, for most of the products
18 that covered their costs in the four- to six-percent
19 range.

20 If your question was whether the pricing
21 function was the origin or was, directed this level of
22 price change, the answer is we received this as a
23 directive.

24 CHAIRMAN GOLDWAY: So you received direction
25 from management --

1 THE WITNESS: Yes.

2 CHAIRMAN GOLDWAY: -- to establish prices
3 within a range.

4 THE WITNESS: Yes.

5 CHAIRMAN GOLDWAY: In your testimony,
6 throughout your testimony you say that there is a
7 general knowledge and expertise in the community and
8 within management about prices. How did you get that
9 information? Top management told you a range, but
10 isn't it -- you said there were a lot of people who
11 work in the field, who are familiar with their clients
12 and familiar with mailers. And somehow that
13 information got to you? How did you get information
14 from the lower level up to your decision level?

15 THE WITNESS: I would say that much of this
16 knowledge, when you use the term in your question "in
17 the field," I think that really what we're talking
18 about is not so much the field as it's used in
19 standard postal discussions, meaning people out there
20 in the various plants. Although there is constant
21 communication between the plants and headquarters.

22 But we're talking mainly with the functions
23 in headquarters, many of the people who work there
24 have come from the field, but the people who,
25 especially those who work with our product and our

1 product management area, they have just continuous
2 contact with, with our customers. They are, they are
3 very well informed about the trends and what's going
4 on in the various industries.

5 And I would point out that the, the head of
6 our Product Management Group is a member of the
7 Executive Committee. He's top management. So these
8 ideas flow horizontally, but they also flow up. And
9 so there's continuous information exchange and
10 discussions that go on, so that upper management,
11 middle management, and other levels are kept apprised
12 of some of these factors that it was discussing in the
13 statement.

14 CHAIRMAN GOLDWAY: Could you better describe
15 the role of product managers? You said product
16 managers.

17 THE WITNESS: Yeah, well, product, when we
18 say product management, we have, we have individuals
19 and functions which are tasked with the
20 responsibilities of managing the various postal
21 products. And I should say also maybe more than
22 postal products; some of our products, some of our --
23 some of the mail we handle may be better addressed by
24 the mail shape.

25 So we may have product managers who focus on

1 products that are let's say predominantly letters or
2 predominantly flats. And so they, they may cover more
3 than one particular product, in a sense that they may
4 focus on flats. And it is their responsibility to see
5 what can be done to manage the profitability of these
6 particular product lines that we have.

7 They're not tasked with operational
8 responsibilities, or necessarily with the financial
9 responsibilities, but they communicate with different
10 functions. Their goal is to try to improve mail
11 volume and profitability, and they communicate with
12 the pricing function. They communicate with other
13 areas to try to see what kind of initiatives we can,
14 we can put forth in order to increase the
15 profitability of the Postal Service, actually within
16 their areas.

17 CHAIRMAN GOLDWAY: So these people who let's
18 say manage flats are charged with dealing with mailers
19 who mail flats, and encouraging increased volume.

20 THE WITNESS: Yes.

21 CHAIRMAN GOLDWAY: But they, then, relate to
22 you what the mailers feel is their price sensitivity?

23 THE WITNESS: They communicated within the
24 Postal Service, yes, they communicated that. They
25 have communicated to me. But I, what I wanted to say

1 is that they communicated within the Postal Service,
2 to senior management, their concerns about the price
3 sensitivity of different mailer groups. And that was
4 what informed the decision by management to request
5 this moderate increase, and to keep it within the
6 range specified.

7 CHAIRMAN GOLDWAY: And after the overall
8 size of the rate increase was determined by top
9 management, you went, as I understand it, you went
10 through the different classes of mail. And the exact
11 amount, the 5.6 percent, was then something that was
12 your discretion, based on advice you got about price
13 sensitivity for different classes of mail, to come up
14 to the 5.6 percent?

15 THE WITNESS: The 5.6 percent was an end
16 result. We were not, we were generally given guidance
17 to develop prices that fell within the four- to six-
18 percent range.

19 Also, for certain products and categories
20 that were, recently haven't been covering their costs,
21 we were given guidance on above, I want to say price
22 increases above the range, or outside of the range.

23 We developed prices that we understood were
24 responsive to, to this particular set of directions.
25 And when we sort of totaled it all up, it came to 5.6

1 percent. So that's where the 5.6-percent number came
2 from. We weren't specifically given that number.

3 Of course, this was communicated with senior
4 management, you know, and it was found to be
5 acceptable.

6 CHAIRMAN GOLDWAY: So if I get it right,
7 then you went sort of class by class, or maybe product
8 by product, and within that range figured out how you
9 were going to allocate the paying.

10 And what factors did you use to shape your
11 decision for each of the classes of mail? We'll go
12 through class by class, but kind of in a general way,
13 how did you use the factors? And how did you use one
14 factor in one class, and another factor in another
15 class?

16 THE WITNESS: Well, we look at, we had some
17 fairly -- we had some fairly tight guidance on that.
18 For example, four to six percent is not a broad range,
19 but it does allow a little bit of leeway. There are
20 some constraints.

21 When we do our pricing, we are required by,
22 required to observe a number of constraints. Some of
23 these are, come out of some of the, let's see, the
24 work-sharing requirements. Some come from the, some
25 of the Commission's directives. For example, in the

1 last annual compliance determination.

2 So these helped us to levels of prices that
3 would respond to the various constraints that we had
4 in addition to the, to the management directive. So
5 we, we also looked at some of the, some of the sort of
6 traditional pricing relationships, where we would try
7 to keep certain price relationships in balance.

8 But then, in addition to that we were given
9 guidance on some other, you mentioned classes of mail.
10 The package services class, for the first time at
11 least that I can recall the package services class as
12 a class failed to cover its costs. And so most of the
13 products in that class got above-average, and I
14 believe outside of the four- to six-percent range,
15 they got increases outside of that range. So we had
16 some guidance there that we should exceed the range in
17 order to try to move that particular class of mail
18 closer to covering its cost.

19 And the same is true with the periodicals
20 class of mail. We were given guidance on that, both
21 with respect to the overall price, but also as to the
22 amount of dispersion that we thought we should allow
23 in developing the prices.

24 CHAIRMAN GOLDWAY: Dispersion?

25 THE WITNESS: The range around the average.

1 Whether it should be close to average or far.

2 CHAIRMAN GOLDWAY: Were you given guidance
3 that everything should be pretty much around the
4 average? Or were you told that you could give wide
5 differences within each class?

6 THE WITNESS: We were asked to keep, we were
7 asked to keep within the range, and generally close to
8 the average, with certain, certain exceptions were
9 allowed.

10 In the case, I mentioned periodicals, we
11 were asked to keep the prices of most categories under
12 10 percent, the price increases under 10 percent.

13 CHAIRMAN GOLDWAY: And small parcels? Were
14 you given guidance on those?

15 THE WITNESS: Yes, we were.

16 CHAIRMAN GOLDWAY: Was that also under 10
17 percent? Or was it --

18 THE WITNESS: No.

19 CHAIRMAN GOLDWAY: What was the percentage
20 for that?

21 THE WITNESS: When you say small parcels, I
22 assume you mean standard mail parcels.

23 CHAIRMAN GOLDWAY: Yes.

24 THE WITNESS: Yes. No, we were given
25 guidance to increase those by larger than 10 percent.

1 And the, we worked with some of the managers in our
2 product management area, and went back and forth with
3 a number of different pricing scenarios, and developed
4 a -- the approximately 23-percent result was, was
5 close enough to the guidance that we were given that
6 it was found acceptable.

7 CHAIRMAN GOLDWAY: I'll ask a question from
8 the ACWU, and then I'll see about my fellow
9 commissioners. This is adapted from an ACWU question
10 1, and also follows, follows up on POIR 3, question 1.

11 In POIR 3, question 1, you were asked about
12 the Postal Service's belief that the electronic
13 diversion of first class single-piece mail was
14 essentially unaffected by price. In the response you
15 discuss the behavior of individuals who send
16 remittances.

17 Did your analysis also examine the behavior
18 of non-household senders of single-piece mail? For
19 instance, businesses that send single-piece mail? And
20 if you did, what did you rely on, and how did it
21 affect your conclusions regarding single-piece mail?

22 THE WITNESS: My understanding is that the,
23 that our conclusions were not sort of bifurcated into
24 an analysis, a separate analysis of parcels versus
25 single piece, but was more of a whole. That the

1 factors that, that we understand were the driving
2 forces behind diversion of single-piece mail to
3 electronic alternatives were not, did not arise from
4 the old price of single-piece mail, but rather were
5 heavily influenced by let's say transactions mailers.
6 And I think some of the information that we have seen
7 suggests that, that some of these forces would not be,
8 would not necessarily affect individuals or households
9 differently than small business mailers, for example.

10 I think I mentioned in my statement that
11 there's a general sort of familiarity and a sense of,
12 there's a great sense of convenience, especially among
13 some of the younger generations, with the use of
14 electronic communications, and a preference for the
15 use of electronic communications over hard-copy mail.

16 This certainly would manifest itself in
17 their decisions to send either personal hard-copy mail
18 letters, or emails or other types of electronic
19 communication. And if they worked in a small
20 business, it would be, I didn't think that we'd see
21 any real difference.

22 I've also seen some research that was
23 prepared for use of the Postal Service by the Boston
24 Consulting Group, where they, in fact, indicated that,
25 if my memory serves me right, that some of the

1 transactions mailers might be more willing to force
2 the issue with businesses than with households.

3 So the part that I saw did not distinguish
4 between larger businesses and smaller businesses, but
5 it may well be that it would flow on down to the small
6 businesses, where they may be more assertive in trying
7 to drive some of this business mail into the
8 electronic channels.

9 CHAIRMAN GOLDWAY: But your decision on
10 raising the single-piece first class mail by two cents
11 and an additional ounce was presuming that first class
12 single-piece mail is unaffected by price.

13 And what we can see is that about one half
14 of single-piece mail is sent by households. The other
15 half, therefore, is sent by a variety of businesses,
16 some large, some small; and that single-piece mail,
17 businesses may have a different sensitivity to price.

18 And are you saying that Boston Consulting
19 Group did a study on businesses, and found out that
20 their single-piece mail is also not affected by price?

21 THE WITNESS: No, I didn't mean to make that
22 assertion.

23 What I was saying is that on the issue of,
24 of the price, the effect of price on volume, there is,
25 of course, the choice of, the price may have an effect

1 on how you send, I would say how much mail you send;
2 but it also may affect whether you send mail at all.
3 Which is sort of like the extreme end of, you know,
4 how much you mail.

5 The Boston Consulting Group information that
6 I saw suggested that, that the decision, or that many
7 transaction mailers were attempting to persuade or
8 otherwise encourage, or perhaps even compel, some of
9 their customers to use electronic forms of bill
10 payment and presentment of payment.

11 And I did not see that there was -- well,
12 what I saw in some of that information was that some
13 of these transaction mailers might be more willing to,
14 in fact, use more persuasive, or to compel the issue
15 with businesses than with single, with households,
16 with consumers.

17 I did not see any research by the Boston
18 Consulting Group that actually measured the price
19 sensitivity of, and let's say the traditional
20 elasticity effect of small businesses versus
21 households. I believe that our forecasting group does
22 our demand analysis. They measure the elasticity for
23 single-piece mail, but they don't differentiate
24 between households and businesses. I don't have a
25 differential.

1 CHAIRMAN GOLDWAY: For businesses, you
2 didn't have a different --

3 THE WITNESS: No.

4 CHAIRMAN GOLDWAY: Was it felt that the
5 availability of Forever stamps would mitigate, to some
6 extent, the price increase reaction for single-piece-
7 mail users?

8 THE WITNESS: Well, the Forever stamp
9 certainly is a, is a convenient way to mitigate some
10 of the difficulties that, that arise from a price
11 change. And it may provide sort of a temporary
12 transition.

13 But I think that the Forever stamp, it
14 provides a convenient way to make a transition.
15 Because over time, the Forever stamp goes up in price.
16 So it's not like the -- unless one stockpiles large
17 quantities of Forever stamps, in which case one could,
18 if they never run out, one could offset the effects of
19 a price change.

20 But what it does is, it's more of a
21 convenience. Because eventually, when one runs out of
22 Forever stamps, one has to go and buy them at whatever
23 the current price is.

24 CHAIRMAN GOLDWAY: So you don't think it
25 affects the elasticity at all.

1 THE WITNESS: I don't know. I haven't
2 studied that. I haven't seen any data on that.

3 CHAIRMAN GOLDWAY: Anyone else want to jump
4 in? Vice Chairman Hammond?

5 VICE CHAIRMAN HAMMOND: I think both of
6 these are in the general category, before we get into
7 specific classes. But, good morning, Dr. Kiefer.

8 THE WITNESS: Good morning.

9 VICE CHAIRMAN HAMMOND: Thank you for being
10 here. I listened to Mr. Neri this morning, and he
11 talked about moving mailers to more efficient behavior
12 of operations to lower costs. And I think these
13 mailers are doing so; yet, they're not necessarily
14 receiving the savings by moving to more automation.

15 Would you say that that is the case? Or
16 would you dispute that? Or, how would you respond?

17 THE WITNESS: Well, we believe that our
18 prices do send signals, and that -- I'm not sure the
19 exact context of, of Mr. Neri's, I'm not sure exactly
20 what he might have meant. But in general, when we
21 have discounts for automation, we believe that they do
22 have an effect.

23 VICE CHAIRMAN HAMMOND: So you would say
24 that they, indeed, end up receiving these savings by
25 moving to more automation. That's essentially what

1 you would say, then, by that?

2 THE WITNESS: If a, the discount that we
3 offer for automation does reflect savings. So if
4 somebody prepares mail such that it's automation-
5 compatible, and we can put it on our automated
6 equipment, they are entitled to whatever discounts are
7 given to that. And so they can enjoy the savings.

8 VICE CHAIRMAN HAMMOND: Okay, all right.
9 Okay. The other thing that I was wondering about, and
10 I asked Mr. Neri the same question. But I was
11 wondering, have you ever designed on your own, or been
12 asked by personnel at the Postal Service, to design
13 anything on any class or subclass of mail that would
14 end up driving mail out of the system because it's
15 supposedly unprofitable to the Postal Service, and the
16 Postal Service would end up losing less money if that
17 particular type of mail left the system? Have you
18 ever looked at that, or done anything towards that?

19 THE WITNESS: I have absolutely never been
20 told to, directed, or suggested, or anyhow been
21 advised to price, develop a set of prices that would
22 drive unprofitable mail out of the system. I've never
23 done that. I've never heard of anything like that.

24 VICE CHAIRMAN HAMMOND: So that's like not
25 even a feasible thought.

1 THE WITNESS: Let me try to give a little
2 context here. We can look at various categories of
3 mail. And if we look at the, at our cost level
4 analysis for 2009, we see that there are certain
5 categories that are indeed failing to cover their
6 costs.

7 But we do not focus solely on the sort of
8 instantaneous, you know, profit or loss of particular
9 categories of mail. I mean, all of the, the products
10 that we now offer, we believe are capable of earning
11 the Postal Service a profit or covering their cost,
12 given appropriate management, over time.

13 And so our goal is to try to achieve that;
14 really to try to get these products to cover their
15 cost. Recognizing that, to the extent that we may
16 increase prices, that the volume may adjust. I mean,
17 that's a fact of life in pricing.

18 But we think that we can bring these
19 products to a position where they will cover their
20 costs, and bring a profit. It will, this is a long-
21 term goal.

22 I think, as I said in the statement, it was,
23 the Postal Service decided that it would not try to
24 force some of these products to get up to the full
25 cost coverage in one step. The Postal Service is very

1 concerned about what impacts the, its pricing
2 decisions can have on its customers. And particularly
3 in this era when there is, there are electronic
4 alternatives available.

5 And I think I mentioned at several points in
6 my statement that the Postal Service is concerned that
7 very large increases in a very short amount of time
8 could push some of these mailers past a tipping point,
9 where this, this mail may disappear. They may decide
10 just they're not going to stay in the mail.

11 So we realize it's an eventual process, it's
12 an evolutionary process. We realize that we don't
13 have forever to do this. But we realize that there is
14 a role pricing can play, and there's definitely a role
15 that efficiencies can play. To close the gap.
16 Profitability is not just a matter of pricing, it's
17 not just a matter of cost. It's the inter-
18 relationship between the two.

19 VICE CHAIRMAN HAMMOND: Okay. Well --

20 CHAIRMAN GOLDWAY: Could you --

21 VICE CHAIRMAN HAMMOND: I was just going to
22 say thank you for your responsive explanation. I
23 don't have any more questions on general, thank you.

24 CHAIRMAN GOLDWAY: Well, it follows directly
25 on this discussion. Which is, could you define for us

1 what the term "rate shock" means in your statement?

2 THE WITNESS: I do use the term "rate shock"
3 in a number of cases. Mainly in conjunction with
4 discussing price changes that would, with relation to
5 certain work-sharing categories. Because this is, in
6 fact, a term in the, in the law and in the PRC
7 regulations.

8 I don't think that rate shock is a term that
9 can be defined absolutely. By saying that this number
10 is rate shock, it's the same number for all products,
11 it is the same number in all circumstances.

12 Rate shock refers to an assessment that a
13 particular price change would cause unacceptable harm
14 or damage to a particular product, or customers for
15 that product.

16 In determining what constitutes rate shock,
17 the Postal Service as a whole kind of looks at a
18 number of factors. It obviously considers economic
19 conditions, general economic conditions. It considers
20 conditions that may be a little bit more particular to
21 the individual category. It looks at the individual
22 mailers who mail within the category.

23 The industry, and whether the industry is
24 healthy or is ailing. All of this, this information
25 is taken into account, and an informed judgment is

1 made as to whether a particular price increase would
2 lead to rate shock.

3 And this, given the fact that this is, as I
4 explained, a bit specific to the set of circumstances,
5 it could change over time. But it also, a level of
6 increase that would constitute rate shock for one
7 product may not necessarily constitute rate shock for
8 another.

9 CHAIRMAN GOLDWAY: Well, one presumption is
10 that a range between four a six percent you determined
11 would not be rate shock.

12 THE WITNESS: In general, yes. That this
13 was, that this would not cause rate shock to the
14 category.

15 CHAIRMAN GOLDWAY: Do you have any specific
16 percentage above which rate shock would be considered
17 likely?

18 THE WITNESS: We would use really a specific
19 judgment based on individual sets of circumstances.
20 So what might be rate shock to one price category of
21 mail may not, in our judgment, be rate shock to
22 another.

23 No, I don't have a specific sort of broad-
24 brush number.

25 CHAIRMAN GOLDWAY: Well, this is a bit of a

1 homework assignment for you. For each discount, where
2 you do assert in your filing the rate shock exception,
3 could you please file with the Commission your planned
4 timeline for phasing out the excess discount?

5 THE WITNESS: We will respond to that, yes.
6 Thank you.

7 CHAIRMAN GOLDWAY: Anyone else want to jump
8 in?

9 COMMISSIONER BLAIR: Madame Chair, thank
10 you. Dr. Kiefer, in your testimony beginning on page
11 53 you discuss the objectives and factors.

12 In reviewing the factor objectives, did you
13 give more or greater weight to some objectives over
14 other objectives and some of the factors, are some
15 more equal than others?

16 THE WITNESS: Well, in general, this is also
17 a case-by-case basis. In responding to the
18 Commission's rules, which require us to show how in
19 particular our price changes help promote the, or
20 respond to the factors and objectives, we interpret
21 this as not meaning that every single price is, needs
22 to, let's say, necessarily promote or respond to, in a
23 particular way, to every single factor and objective.

24 So to the extent that we look at this as
25 overall, that our prices do help, let's say, promote

1 the factors. But we may be, that doesn't necessarily
2 mean that you could take every single price of the
3 thousands of prices we offer, and say specifically how
4 this particular price promotes factor X more than,
5 more than this other price cell, or promotes factor X
6 more than factor Y. It's more generalized.

7 COMMISSIONER BLAIR: The reason I'm asking
8 that is that we had a previous discussion regarding
9 flats. And I just was wondering how much of a
10 priority on cost coverage the Postal Service, what
11 kind of priority or premium on cost coverage does the
12 Postal Service place?

13 THE WITNESS: A very high priority,
14 Commissioner Blair. We are, we are very determined to
15 see that our flats products move toward covering their
16 costs.

17 At the same time, I think I mentioned this
18 in some of the earlier discussion, that we're looking
19 out over time. We're concerned. I mean, some of
20 these products might need a 15- or 20-percent increase
21 in order to cover their costs.

22 We determined that that probably would be
23 counter-productive, to try to reach all the way to
24 full cost coverage in one step. The fact that we did
25 not propose prices that went all the way to covering

1 the costs does not in any way mean that we, we don't
2 consider that a very high priority.

3 COMMISSIONER BLAIR: I think this is more of
4 a statement than a question. But where I'm concerned
5 is that cost coverage is an objective, I'm sorry, a
6 factor in the Act. But it seems to me that it's
7 always achieved by increasing rates. And I am just as
8 concerned that costs be addressed that bring rates,
9 that can achieve the current, that can achieve lower
10 rate increases.

11 And so I want to make sure that -- my
12 concerns are the balance between the two. But I also
13 noticed on page 58 of your statement, you said that
14 price change is important to consider in the long
15 term, rather than simply focusing on this year's
16 prices in isolation.

17 My view of an exigency is that it's an
18 emergency, and it addresses a short-term need. You're
19 saying it addresses a long-term need? And is this a
20 structural issue that you're invoking? Or as a basis
21 of the, for a basis of the exigency?

22 THE WITNESS: As I understand your question,
23 well, let me try to answer that, and then you can tell
24 me if you think that I've addressed your concern.

25 Well, it's clear from the statements of Mr.

1 Corbett and Mr. Masse that our needs for revenue are
2 very much a, sort of a near term; that my
3 understanding is we may not, if we do not get some
4 relief -- which can come from several areas; one you
5 mentioned was reduction in costs, others are increase
6 in revenues -- the Postal Service could find itself
7 unable to, to meet its obligations.

8 COMMISSIONER BLAIR: We had a discussion
9 about this over the last two days, that even with,
10 should the price, an exigency be found, and the price
11 increases be granted, it's not sufficient to meet the
12 cash flow needs in 2011 or 2012.

13 THE WITNESS: That is an area, getting into
14 that level of detail is really beyond what I --

15 COMMISSIONER BLAIR: I understand that, but
16 we had this discussion over the two days, and the
17 postal witnesses acknowledged that. So I'm trying to
18 put into place -- and you brought it up in your
19 testimony -- about how this exigency is addressing a
20 long-term need, or is considering the long term, and
21 not simply focusing on the year's prices.

22 THE WITNESS: Right.

23 COMMISSIONER BLAIR: And I see a disconnect,
24 or I don't understand that.

25 THE WITNESS: Okay.

1 COMMISSIONER BLAIR: I thought it's more to
2 address a short-term need.

3 THE WITNESS: Let me tie, let me try to tie
4 that statement together, and maybe that will satisfy
5 you. When I talked about the long-term need -- well,
6 first of all, the fact that we are requesting an
7 increase at the level of, on average, of 5.6 percent
8 is, does try to sort of push revenues up faster than
9 we think our costs will go. So this will try to cover
10 part of the need.

11 But the discussion of the long term
12 generally in my statement was to focus that when we
13 choose how far we go in our pricing, we always have to
14 have the long term in mind. Because trying to solve
15 the problem by let's say increasing the overall prices
16 by 20 percent, which is probably on the order of
17 magnitude we may have needed, might have damaged our
18 customer base. And we really are concerned that this
19 could do that.

20 In the long term, it would not be wise that
21 if we felt that we could get a big burst of, of
22 revenues from an extremely high price increase, but
23 then sort of accelerate it and cause the erosion of
24 mail volumes such that we would end up destroying the
25 business.

1 So the long term is, in some sense, a factor
2 that constrains us from solving the whole exigent need
3 solely by raising prices. Does that connect that for
4 you?

5 COMMISSIONER BLAIR: Well, it does, and
6 again, it sets off concerns with me that I think the
7 cap right now is about .76.

8 THE WITNESS: Yes. I think we have --

9 COMMISSIONER BLAIR: Or 5.78, I'm sorry. A
10 little over half a percent.

11 THE WITNESS: Yes, yes.

12 COMMISSIONER BLAIR: So you're proposing
13 to -- my math is terrible. But you're proposing to
14 raise prices 10 times that of the cap, basically. So
15 that fits in the long-term interest of the Postal
16 Service?

17 THE WITNESS: Well, we take this step
18 reluctantly.

19 COMMISSIONER BLAIR: I think maybe that's an
20 unfair question. That's a question that the
21 Commission has to address.

22 THE WITNESS: Right. But certainly --

23 COMMISSIONER BLAIR: To me, that's 10 times
24 what the cap would be at a time when, if you've read
25 the headlines the past few days, the stock market is

1 again plummeting today; there is a risk that the
2 recovery is stalling. And where I'm coming from is
3 saying and we're going to break the cap, and we're
4 going to do it by 10 times, to address short- or long-
5 term needs, is something that I'm still trying to get
6 my head around.

7 THE WITNESS: Right. Well, I think the
8 situations that you mention certainly are, are factors
9 that lead us to, that lead us to believe that any
10 increase in our prices needs to be moderate. And I
11 realize that, you know, I'm not going to dispute your
12 math; it may be a fairly high ratio.

13 COMMISSIONER BLAIR: The 5.78 I believe was
14 based in Postal Service testimony. I want to say it's
15 about three quarters of a percent, so my math may be
16 somewhat off. But I think it's still, if it's nine or
17 seven or five, five times the rate of what is
18 permitted already under law, and by busting the cap to
19 do so, is something that I'm still, I'm still troubled
20 with. And I appreciate your answers on this.

21 THE WITNESS: Could I continue to address
22 this? I realize this is a serious concern for the
23 Commission.

24 The ratio looks very high. And that is, of
25 course in part, because the actual level of CPI

1 inflation is pretty low.

2 Taken as a difference, the number, we're
3 asking for something that is maybe on the order, maybe
4 just a little bit under, four to five percent over the
5 cap.

6 And when we think about this, I think it is
7 important for the Commission to keep in mind that we,
8 we are proposing these prices to go into effect in
9 January of 2011. Our last price change was in May of
10 2009. I think that's about -- and I will also confess
11 to not having a calculator-like mind -- but I think
12 that's about 19 or 20 months.

13 And I think that when we take that, that 5.6
14 percent, and we sort of annualize it, the actual
15 increase is something between maybe around three to
16 three and a half percent.

17 So on an annualized basis, we are asking,
18 we're asking for more than the rate of inflation. But
19 we are also trying to keep it as moderate as we could.

20 COMMISSIONER BLAIR: I understand the
21 difficult position you're in. I just hope that you
22 understand the difficult position you're asking
23 customers to bear at a time that their costs are
24 increasing.

25 THE WITNESS: Absolutely. Absolutely.

1 COMMISSIONER BLAIR: And their businesses
2 are shrinking, and the burden that would be placed on
3 them by an increase like that. And that's more of a
4 statement than a question.

5 THE WITNESS: Well, I was just going to say,
6 speaking of statements, I hope that one message that
7 came across loud and clear in my statement was our
8 concern that these price increases might have on our
9 customers.

10 I mean, I think it came out over and over
11 again that we are really concerned about our
12 customers. And at the same time, we're concerned
13 about paying the bills.

14 COMMISSIONER BLAIR: Thank you.

15 CHAIRMAN GOLDWAY: Commissioner Langley.

16 COMMISSIONER LANGLEY: Thank you. And thank
17 you, Dr. Kiefer, for being here today. Please be
18 assured that your concern about over-pricing and, you
19 know, the interest in your direct testimony, that your
20 noticing what's happening with your customers comes
21 across well.

22 In fact, I was intrigued by your discussion
23 on page 13 of your testimony. You talked about the
24 tipping point of large first class mailers.

25 And I had read your testimony in preparation

1 for Mr. Corbett and Mr. Masse, and asked both of them
2 whether they believed the decline in after-rate volume
3 estimates adequately reflected the reality of today's
4 economic environment. And both said that there was a
5 great deal of reliance on historical information as
6 far as how customers would react to pricing increases.

7 And I think your statement is a better
8 reflection, perhaps. And I don't think that you're
9 intending to contradict them at all.

10 But I'm curious whether or not you believe
11 that the volume declines estimated are really
12 reflecting the reality of today's environment.

13 THE WITNESS: When you say the volume, are
14 you referring to the volume responses to our price
15 changes contained in Mr. Masse's statement?

16 COMMISSIONER LANGLEY: Yes, I am.

17 THE WITNESS: Okay. Yeah, I think I can,
18 again, try to put a little context in that.

19 I know that Mr. Masse's analyses used our
20 elasticities, price elasticities from our forecasts,
21 our demand models. These are, of course, as all
22 econometric equations are, they're based on historical
23 data. They remain the best information we have. And
24 this is, this is what we have to use.

25 I think the discussion on page 13 and around

1 that section of my testimony was, was designed to
2 discuss what could happen if we went well out of the,
3 let's say the -- first of all, if we went well beyond
4 the sort of, the type of historical experience that we
5 had.

6 Now, I mentioned a little bit earlier that
7 there were some who thought that, well, we should
8 raise prices to cover the costs. And you know, if it
9 was, it might take 15 to 20 percent or something like
10 that. You know, I think a 20-percent increase for all
11 mail is not something that lies within the recent
12 historical experience of, you know, the Postal
13 Service.

14 So in that sense, when we're dealing with,
15 let's say, a potential impact of a hypothetical
16 increase that, of that size, the elasticities may not
17 provide as good guidance as they might if we were
18 dealing with something that is much closer to the
19 range. And I would say that price increases of five
20 percent or so I think are within the historical range
21 that some of these equations were estimated using.

22 My recollection is that, sort of in the old
23 former Rate Case days, we would wait two or three
24 years before changing prices. And we would get price
25 changes, you know, easily, within the four-, five-,

1 six-percent range.

2 So I would, I think that we want to look at
3 this in two ways. One is to say that the price
4 changes we are proposing are not unprecedented. And
5 the, we wouldn't necessarily feel that we should
6 discard the elasticity information.

7 On the other hand, when we start going much
8 higher, if we say that well, why didn't you raise the
9 prices, you know, 10, 15, 20 percent; well, then we
10 are concerned that perhaps some of this, I called it
11 tipping point effect might occur.

12 So I'm not sure that the two are necessarily
13 totally opposed to each other, you know.

14 COMMISSIONER LANGLEY: So if the economy
15 were to contract rather than to expand, as is the
16 expectation of the Postal Service in this particular
17 analysis, would it be possible at all to even estimate
18 volume decline?

19 THE WITNESS: Well, I --

20 COMMISSIONER LANGLEY: I think I may be
21 asking an impossible question.

22 THE WITNESS: Well, it's perhaps as question
23 I would, I would want to consult with our forecasting
24 people on. But in general, I mean, there is some
25 volume -- excuse me, some economic growth factored

1 into this. Generally, economic growth leads to, to
2 more mail volume, and more revenue.

3 So I would think that it would not be a
4 positive development if, if the economy contracted
5 compared with what we had assumed in Mr. Masse's
6 exhibits.

7 COMMISSIONER LANGLEY: Thank you. And let
8 me just ask a final question right now. Obviously,
9 you, I think you very much appreciate that these price
10 increases proposed have real meaning to the businesses
11 that are impacted by them.

12 THE WITNESS: Absolutely.

13 COMMISSIONER LANGLEY: What quantitative
14 analysis does the Postal Service do to determine what
15 segments of the industry might be more delicately
16 situated right now than others?

17 THE WITNESS: Well, I heard this question
18 asked in a number of contexts. We don't generally
19 find, it's rather difficult to do numerical analyses
20 on these. We don't have data, and in many cases,
21 virtually all cases I know, our judgment about which
22 segments are more delicate than others, it's an
23 informed judgment. It's based upon considering the,
24 you know, the individual segments, the economic
25 conditions, the other, other factors.

1 It does take into account what information
2 we have from estimated elasticities. But in the end,
3 it's an informed judgment. It's not something that
4 we, we found a bunch of data, and put it into a model,
5 and turned the crank, and it said okay, this segment
6 is more delicate than that. There is --

7 COMMISSIONER LANGLEY: It's a qualitative
8 analysis.

9 THE WITNESS: It's a qualitative analysis
10 based on informed judgment, yes.

11 COMMISSIONER LANGLEY: Do you look at volume
12 declines?

13 THE WITNESS: Well, yes. I mean --

14 COMMISSIONER LANGLEY: What factors go into
15 it as you're looking at it?

16 THE WITNESS: Well, as I said before, the
17 general economic conditions. And we also look at the
18 individual product information. We have revenue and
19 volume information on the product. And if products
20 are losing volume, well, that's a clear sign that
21 there is, that this is in a precarious position.

22 And we also look at factors like what some
23 of the alternatives are. Is this just something
24 that's going to go down with the economy and bounce
25 right back with the economy? Or is it something that

1 is susceptible to electronic diversion, and could
2 just, you know, the volume's going to go down and
3 never come back.

4 COMMISSIONER LANGLEY: Does the Postal
5 Service go beyond and look at economic forecasts, both
6 short- and long-term, for a particular industry? See
7 what outside analysts might be saying?

8 THE WITNESS: Yes. Well, certainly we look
9 at economic forecasts. And we also -- yes.
10 Especially the people in the product management are
11 continually monitoring the industry media, you know,
12 the trade press and others. And they see this kind of
13 information, that forecasters, people say this is
14 going to grow, or this is not going to grow, or
15 whatever.

16 COMMISSIONER LANGLEY: Do you have meetings
17 among the staff you say who monitor these things?
18 Product managers and your pricing people, and you go
19 class by class or product by product? Do you discuss
20 these things?

21 THE WITNESS: Well, I would say --

22 COMMISSIONER LANGLEY: Is there a structured
23 way to go about this? You're kind of, everything is
24 very general and amorphous in your descriptions. Is
25 there a structured way to make these decisions?

1 THE WITNESS: You mean as to the -- well, as
2 I said at the beginning, we were given a directive
3 that constrained the price changes for most products
4 into the, a narrow range of four to six percent.

5 There certainly were discussions made,
6 generally between, since the, since the impetus or the
7 general guidelines were made by senior management,
8 much of the discussion with the product management was
9 between, well, between the product managers and senior
10 management.

11 COMMISSIONER LANGLEY: So did they tell you
12 we want an eight-percent raise for periodicals? You
13 know, we want a five-percent raise, you know, under
14 the reg, for standard flats? Did they give you those
15 specific directions?

16 THE WITNESS: My understanding is, for
17 periodicals, eight percent was --

18 COMMISSIONER LANGLEY: What you were told.

19 THE WITNESS: -- we were told. How far, how
20 far would be acceptable as a deviation, I'm talking
21 now not for individual cells within the range, but for
22 how far the averages could deviate from that and still
23 be acceptable.

24 I don't know. We presented eight percent,
25 and it was accepted.

1 COMMISSIONER LANGLEY: And the presumption
2 that standard flats was a delicate industry and needed
3 some caution in its rate increase was something that
4 was given to you. You didn't participate in meetings
5 where your, the people who have knowledge and
6 expertise and you, the pricing people, met together to
7 decide on this?

8 THE WITNESS: Well, let me -- I'm aware that
9 a case was made to give, that standard mail flats was
10 a particularly delicate, in a particularly delicate
11 situation; and that it should receive a lower range of
12 price increase.

13 In the end, the considered judgment of
14 management was that it should stay within the range.
15 That it should be in the range of very close to five
16 percent, in the middle of the range.

17 COMMISSIONER LANGLEY: So upper management
18 has been giving you pretty clear direction as to what
19 the price increases should be.

20 THE WITNESS: Well, we were given a range,
21 and it was, it was fairly clear. And we were allowed
22 to propose prices that sort of fell within the range,
23 and in some cases, that the direction was a little bit
24 more explicit.

25 COMMISSIONER LANGLEY: So with regard to

1 flats, and your response to POIR-3, question 2, that
2 you said the Postal Service did not rely on studies or
3 analysis of the industries that send flat-shaped mail
4 in various classes, just to determine the size of the
5 increase that each could tolerate.

6 Instead, you said that you relied on
7 knowledge gained from meetings with mailers,
8 conferences, and trade press coverage of the industry.
9 Were those meetings you were part of?

10 THE WITNESS: No.

11 COMMISSIONER LANGLEY: And how much of that
12 information, if you don't know, how much of it came
13 from sources that are not directly affected by those
14 rates? In other words, did management do any external
15 surveys, or seek guidance from something other than
16 talking to the users of flats? Non-industry sources
17 of information.

18 THE WITNESS: Oh, you mean -- would you
19 discount, for example, the trade press? Do you mean
20 to exclude those?

21 COMMISSIONER LANGLEY: Yes. The things not
22 directly related to the --

23 THE WITNESS: Okay. I can't address that
24 specific question. I mean, I don't know the answer.

25 COMMISSIONER LANGLEY: So the case for how

1 delicate flats, as a class, were, was made at a higher
2 level? When you were looking at deciding well, it
3 should be five percent, did you have some information
4 about flats that you were using? How did you get that
5 information?

6 THE WITNESS: I was asked to come up with a
7 set of prices that were in the, generally in the five-
8 percent range.

9 The evaluation as to, as to what these, as
10 to the initial goal, or the five percent, was based
11 upon a discussion, which I was aware of. But I mean,
12 I was not in the middle of it.

13 All of the, the individuals who were
14 involved, have familiarity with the customer areas and
15 the segments and the industry. How much of it came
16 from -- well, as I said, some of the information came
17 from mailers. And they are obviously an interested
18 party. Some of it comes from news media that report
19 on these industries.

20 And I don't see a particular reason why they
21 would not be considered a survey, a disinterested
22 reporter of the facts. I mean, in other words, I
23 don't think this was just from lobbying groups. This
24 was, you know, the people who monitor the industry.

25 And there's a real value in getting accurate

1 information. And so if a particular consulting group
2 does a study, and says that such-and-such, a
3 particular type of advertising is going to go up or go
4 down, then it gets reported. And our people monitor
5 that, and use it to make their judgments.

6 COMMISSIONER LANGLEY: I see. Okay.

7 THE WITNESS: It wasn't just, I didn't mean
8 to convey that this was just we were talking to
9 specific mailer groups only.

10 COMMISSIONER LANGLEY: Well, I certainly
11 don't deny that you should talk to mailer groups in
12 this area.

13 THE WITNESS: Oh, no, we get a lot of --

14 COMMISSIONER LANGLEY: Information is very
15 useful and helpful. I just wanted to get a sense of
16 the range of information that you were able to
17 consider.

18 When you were asked about first class mail
19 and were told the four to six percent, were you told
20 two cents? Because, you know, you could have come up
21 with a one-cent increase and other rates within the
22 class. Were you told specifically two cents?

23 THE WITNESS: Well, we started out with a
24 two-cent increase because that was, that was the
25 particular change allowing for the convention that we

1 place the first-class stamp in whole cents.

2 The two-cent increase was the increase that
3 got us within the range. And although I believe that,
4 well, I mean, that was what we started with. And I
5 think that --

6 COMMISSIONER LANGLEY: So you never did
7 experiment with --

8 THE WITNESS: With the one cent?

9 COMMISSIONER LANGLEY: With the one cent and
10 the other options that would fall from there?

11 THE WITNESS: No. We didn't --

12 COMMISSIONER LANGLEY: Like 45 cents, you
13 know. A clear number.

14 THE WITNESS: Certainly no detailed analysis
15 was done. We started out with the two-cent increase.
16 I won't say that nobody at any time wondered about a
17 45-cent stamp. But we started out, because it was, it
18 fell within the range. And we thought that this was
19 an appropriate increase.

20 COMMISSIONER LANGLEY: Just for the record,
21 I'll say that consumers would, I think, pay more for a
22 second ounce and a third ounce if they all fit neatly
23 into nickels and dimes, and they could remember them
24 all.

25 THE WITNESS: Duly noted.

1 COMMISSIONER BLAIR: Could I just issue a
2 clarification for the record?

3 COMMISSIONER LANGLEY: Sure.

4 COMMISSIONER BLAIR: When we were talking
5 about the CPI caps, I believe in the Postal Service's
6 testimony you had a half a percent?

7 THE WITNESS: Five-seven-eight I think was
8 the number that I recollect.

9 COMMISSIONER BLAIR: Right, five tenths, six
10 tenths. And according to the Commission's web site,
11 as of the 16th of July, we'll be posting a new one in
12 the next week or so, we're at .968.

13 THE WITNESS: Okay.

14 COMMISSIONER BLAIR: So just for
15 clarification purposes, that's still five to six
16 times --

17 COMMISSIONER LANGLEY: And with the banked
18 amount, we're pretty much at one percent.

19 THE WITNESS: Okay. Thank you.

20 COMMISSIONER LANGLEY: That's interesting.
21 A specific question here. With regard to your
22 response to POIR-3, question 4, you identified the
23 source of retained pre-sort volume of 53 million
24 pieces is based on management judgment.

25 Again, could you elaborate on your

1 management judgment? I mean, why was it 53 million
2 pieces, as opposed to, say, 50 million pieces? This
3 is for free reply, reply writes free program.

4 THE WITNESS: Okay. I'm sorry, did you say
5 POIR --

6 COMMISSIONER LANGLEY: POIR-3, question 4.

7 THE WITNESS: -- 3, question 4. The copy I
8 have here has four -- has several subparts.

9 CHAIRMAN GOLDWAY: I don't know that I have
10 a page number on it. Question 4, Response A, just
11 before the Response B.

12 THE WITNESS: Okay.

13 CHAIRMAN GOLDWAY: At the end of A, if they
14 retain --

15 THE WITNESS: I see it. This is a
16 definition then.

17 CHAIRMAN GOLDWAY: And in your report, you
18 have indicated that it will be 53 million pieces. So,
19 we wanted to get a better sense of how you calculate
20 these numbers.

21 THE WITNESS: Okay. I can attempt to find
22 that out for you, but I don't know. I didn't do that
23 particular calculation.

24 CHAIRMAN GOLDWAY: Would you please?

25 THE WITNESS: Yes.

1 CHAIRMAN GOLDWAY: Thank you. Do you have
2 another question?

3 COMMISSIONER ACTON: Yes. Good afternoon,
4 Dr. Kiefer.

5 THE WITNESS: Good afternoon.

6 COMMISSIONER ACTON: Thank you for being
7 here with us. It is a little awkward in how we are
8 approaching some of these questions, but just so you
9 know, this is a new format, and hopefully it will stay
10 novel.

11 But we are working through it by trying to
12 incorporate in our inquiries some of the community's
13 important questions, and we are all sort of taking
14 turns at that opportunity, all right?

15 THE WITNESS: Okay.

16 COMMISSIONER ACTON: But before I do that, I
17 have a question. How long have you been a pricing
18 economist at the Postal Service?

19 THE WITNESS: Almost 12 years.

20 CHAIRMAN GOLDWAY: So you were at the
21 Service doing pricing and setting rates when the
22 reform was enacted in 2006?

23 THE WITNESS: That's correct.

24 COMMISSIONER ACTON: Are you familiar with
25 the law and statutes as it goes to pricing?

1 THE WITNESS: You are referring to the new
2 law or the old law?

3 COMMISSIONER ACTON: I am referring to the
4 Postal Accountability Enhancement Act.

5 THE WITNESS: Somewhat. I mean, I am not an
6 attorney.

7 COMMISSIONER ACTON: Sure. Neither am I.
8 When the Act was formulated, I think there is a
9 provision that calls for the Service to be able to
10 invoke one last opportunity for an Omnibus Rate Case.
11 Do you know that?

12 THE WITNESS: Yes, I remember that.

13 COMMISSIONER ACTON: Do you know if there
14 were discussions at the Service at the time about the
15 provision in the statute that allowed for that, and
16 what the thoughts were at the management level?

17 THE WITNESS: Well, ultimately the decision
18 was made -- and this is my recollection. At the time,
19 we were awaiting the publication of the Commission's
20 rules, which came out in Order Number 43, and my
21 understanding was that we were waiting to see how the
22 rules were, and that was one factor that led to our
23 decision whether to file the final old style rate case
24 or not.

25 But once the Commission's rules were filed,

1 management made its judgment, and decided that it
2 would not use the old format. I was not part of that
3 decision.

4 COMMISSIONER ACTON: The reason that I am
5 inquiring is that I am not privy to the background of
6 why the Legislators decided that it was important to
7 include that provision in the new law, but one guess
8 might be that they were anticipating that the Postal
9 Service management would look at the requirements of
10 the law in its totality as far as what sort of costs
11 and expenses would be called for going forward,
12 including these new workforce obligation expenses and
13 what not.

14 And that they might take the opportunity, or
15 at least give an assessment on whether or not they
16 would be able to management to adequately cover those
17 costs without having to dramatically or even
18 indramatically reset the rate structure.

19 THE WITNESS: As I said,. the decision was
20 made by senior management, and I do not know all of
21 the factors, or all of the weights, that went into
22 that decision.

23 COMMISSIONER ACTON: I appreciate that, and
24 I understand that there is some decision making going
25 on that may not always be in your office.

1 THE WITNESS: Yes, quite a bit.

2 COMMISSIONER ACTON: But my bottom line
3 point on that is that I am just trying to understand
4 if the Service reviewed all of these costs, and
5 anticipated that they didn't need to file the Omnibus
6 case because they were expecting that they would be
7 able to work under the new rate cap regime to meet
8 these obligations.

9 THE WITNESS: Well, one thing that we have
10 to keep in mind is that if we chose to file a final
11 rate case under the old scheme, it would have to be as
12 all the other PRA rate cases would be a break even
13 case.

14 So there wouldn't be any opportunity for us
15 to sort of stockpile funds against the possibility
16 that maybe 3, 4, or 5 years down the road that we
17 would face difficult circumstances.

18 COMMISSIONER ACTON: No, I wasn't talking
19 about stockpiling excess funding.

20 THE WITNESS: Okay.

21 COMMISSIONER ACTON: I was talking about the
22 veracity of forecasting, and the hazards involved in
23 trusting projections that in some cases may not be
24 very accurate.

25 THE WITNESS: Well --

1 CHAIRMAN GOLDWAY: Or the ability to cover
2 costs.

3 COMMISSIONER ACTON: And I know that the
4 Chairman is preparing to adjourn or to break for
5 lunch, but I have one more of our questions from a
6 POIR, and also I just want to clarify, that when
7 Commissioner Langley is talking about her worries
8 about elasticities, and the Service is bringing a case
9 which bears upon proving that this is an extraordinary
10 and exceptional circumstance, if the Commission buys
11 that, and we end up implementing some of these rates
12 that you are proposing, how can we not expect that
13 perhaps in an extraordinary and exceptional
14 circumstance price elasticity that products may
15 respond to that in an extraordinary and exceptional
16 fashion, meaning --

17 THE WITNESS: I understand. All I can say
18 is that we have a better chance of seeing more typical
19 behavior with a more moderate increase than we would
20 if we have one that was sort of unprecedented.

21 COMMISSIONER ACTON: Okay. That's fair.
22 Here is a followup to a Presiding Officer's
23 Information Request Number 3 was question two.

24 THE WITNESS: Question two. Okay.

25 COMMISSIONER ACTON: And it is for

1 information --

2 CHAIRMAN GOLDWAY: No, I think we did that
3 one.

4 COMMISSIONER ACTON: Did we do that one
5 already?

6 CHAIRMAN GOLDWAY: This is the one from GCA.

7 COMMISSIONER ACTON: Oh, here we are. I'm
8 sorry. This is adapted from a GCA Question Number
9 33A. The Postal Service proposes a one cent increase
10 in the additional ounce rate for single piece flats
11 and letters, for non-automation presort letters and
12 flats, and for automation flats.

13 In contrast, no increase is proposed for
14 additional ounces of single piece parcels, presort
15 parcels, and automation letters. Can you please
16 explain the reasoning behind this aspect of your
17 proposal, including the reason for creating a new
18 distinction between additional ounce for single piece
19 letters and parcels?

20 THE WITNESS: In one respect, I think one of
21 the main factors that led us to moderate the price for
22 -- or for the additional ounce price for first-class
23 parcels was also part of our proposal for first-class
24 parcels was a change, such that the first three ounces
25 would receive a fairly -- well, it would all have the

1 same price.

2 That meant that one ounce parcels would now
3 pay the same price as three ounce parcels; and two
4 ounce parcels, what would now paid a different price,
5 would now pay the same as three ounce parcels.

6 That led to a significant increase, and in
7 order to -- we recognize that many of our mailers mail
8 a range of parcels. So, in other words, it is not
9 necessarily people only mailing two ounce parcels.

10 Some people mail two ounce parcels, and mail
11 four ounce parcels. So the moderation of the
12 additional ounce price for parcels was designed to
13 sort of work together to maybe mitigate some of the
14 impact of increasing the zero to one, and one to two,
15 ounce prices to match that of three ounces.

16 So we would keep prices for parcels that
17 were a bit above the three ounce range so that they
18 didn't have such a large increase. So mail over that
19 sort of that light weight range -- you know, one, to
20 two, to three ounce parcels, and four ounces, and five
21 ounces, would have a bit of a mitigation there.

22 COMMISSIONER ACTON: Okay. I think that
23 wraps -- I'm sorry.

24 CHAIRMAN GOLDWAY: I just wanted to ask more
25 on that. I forget the number, but the rate increase

1 for that single ounce parcel --

2 THE WITNESS: For the zero to one ounce
3 parcel?

4 CHAIRMAN GOLDWAY: The zero to one ounce
5 is -- well, 50 or 60 -- well, what is the percent? It
6 is really a significant rate increase.

7 THE WITNESS: Well, yes, it is a significant
8 rate increase.

9 CHAIRMAN GOLDWAY: Somewhere between a 30
10 and 50 percent increase in price. That is not rate
11 shock?

12 THE WITNESS: Well, as I said -- well, let
13 me explain. We were concerned that the lightest
14 parcels mailed and that were priced, or that were zero
15 to one ounce, were not adequately covering their
16 costs.

17 And as I said, we looked at the parcel
18 prices, with the goal of trying to come up with a
19 pricing that over a reasonable range would be
20 appropriate. Now, if you only mailed zero to one
21 ounce parcels, you would be seeing a fairly large
22 increase, although the absolute price would be -- it
23 is not extremely large. Let me see if I can find it.

24 (Pause.)

25 THE WITNESS: Well, for a retail one ounce

1 parcel, our proposed price is \$1.71, and we have to
2 remember that with this comes the ability to mail
3 something anywhere in the United States for \$1.71.

4 CHAIRMAN GOLDWAY: And what is the cost
5 coverage when you go up to \$1.71 for three ounces?

6 THE WITNESS: I'm afraid that we don't have
7 cost -- well, I am sure that we don't have cost
8 coverages by ounce, but I am not sure what the cost
9 coverage is for the parcels. The prices that we were
10 giving were actually for retail parcels, which is the
11 higher parcel price. I mean, higher than our
12 commercial parcels.

13 COMMISSIONER ACTON: Dr. Kiefer, I have a
14 followup question, please, from our Agency analyst.

15 THE WITNESS: Sure.

16 COMMISSIONER ACTON: They would like to know
17 if you are maybe planning or intending to set letter
18 and parcel, additional ounce, at the same price at
19 some time in the future, or if you would keep them
20 different?

21 THE WITNESS: I am sure that it is something
22 that would be considered. There isn't at this time --
23 I don't think there is an explicit intent, let's say,
24 one way or the other. I mean, it is something -- I
25 mean, the additional ounce price is one that often

1 varies.

2 It sort of is traditionally a --
3 traditionally, it is something that has been used to
4 sort of take up the slack sometimes, and if the first
5 ounce price goes up quite a bit, sometimes the -- and
6 as I say, the additional ounce price has been used to
7 sort of offset some of the impact of the lumpiness
8 that is caused by the -- you know, by the whole cent
9 constraint.

10 COMMISSIONER ACTON: Thank you.

11 CHAIRMAN GOLDWAY: Okay. I think we have
12 had a long morning, and we expect to have a long
13 afternoon. We have many more questions for you on
14 periodicals and standard package services, and special
15 services.

16 So what I propose is that we break for
17 lunch, and we return at two o'clock sharp. Thank you.
18 This meeting is adjourned until 2:00 p.m.

19 (Whereupon, at 12:48 p.m., a luncheon recess
20 was taken.

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25 CHAIRMAN GOLDWAY: Yes, the number of co-
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1 mailings, and the pieces co-mailed, and bundled co-
2 mailed, and pallets containing co-mailed flats and/or
3 bundled?

4 THE WITNESS: I don't know the extent of the
5 data that is available to address that.

6 CHAIRMAN GOLDWAY: We would really like to
7 know what kind of data the Postal Service keeps, and
8 if it does, to obtain it in some form. The point is
9 that catalog and periodicals mailers believe that they
10 have become more efficient, and that they followed
11 directions and in some cases encouraged the Postal
12 Service to implement procedures to co-mail and develop
13 pallets, and get out of stacks.

14 And yet they are receiving a higher than
15 average percentage price increase, and standard plus
16 gets a price increase that is below the average. And
17 there seems to be some question of fairness that they
18 would like to have us explore.

19 THE WITNESS: Okay.

20 CHAIRMAN GOLDWAY: Whatever information you
21 can provide with regard to data --

22 THE WITNESS: On co-mailing?

23 CHAIRMAN GOLDWAY: Yes, on co-mailing for
24 periodicals is what we would like. And then can you
25 answer why did the CRA unit cost of periodicals mail

1 increase by more than double the rate of inflation
2 between 1996 and 2009, despite the deployment of the
3 AFSM-100, and the increased amount of work sharing
4 performed in the periodicals class?

5 THE WITNESS: I'm afraid that is beyond a
6 pricing scope.

7 CHAIRMAN GOLDWAY: It seemed to be something
8 that we could ask Mr. Neri either. Do you know who we
9 might ask?

10 THE WITNESS: The analysis of cost --

11 CHAIRMAN GOLDWAY: CRA cost data, and unit
12 cost for periodicals went up 54 percent in that 15
13 year period. The CPI went up 37 percent.

14 THE WITNESS: Right. In pricing, we take
15 the CRA as an input. That is produced in finance. If
16 I were to ask that question, they would be the ones
17 that I would ask.

18 CHAIRMAN GOLDWAY: Is there a particular
19 person in finance that we should direct this to?

20 MR. RUBIN: I think the finance staff is
21 aware of this question, and so I can push them to get
22 some response. It is a pretty complicated question,
23 but we can provide what we can find out.

24 CHAIRMAN GOLDWAY: Okay. So there are three
25 questions here on behalf of intervening parties with

1 regard to the basic issue of why costs continue to go
2 up, and go up more than inflation, when the
3 periodicals class has implemented itself and with the
4 AFSM-100, significant automation and efficiency
5 improvement.

6 And we want any data that we can on the
7 number of periodicals that can be tracked for having
8 co-palletization, or other kinds of automation that's
9 possible, and any explanations in finance as to why
10 these costs go up so much more than the cost of
11 inflation.

12 The reported unit cost for delivery for
13 periodicals flats, and standard flats mail, increased
14 by 24 percent and 36 percent, respectively, between
15 2007 and 2009 alone. And we don't seem to have
16 answers. Now, a question for you, Dr. Kiefer.

17 THE WITNESS: Okay.

18 CHAIRMAN GOLDWAY: When you were asked about
19 preparing these rates did you think about waiting to
20 increase the periodicals rate disproportionately as
21 was recommended to you in advance of the completion of
22 the periodical study that has been mandated by
23 Congress?

24 Were you aware of that periodicals study?
25 What was the thinking in not waiting for that study?

1 THE WITNESS: Well, yes, I was aware that
2 the periodical study was going on, but we were also
3 aware that under the current law that the only
4 opportunity that we have to increase periodicals, or
5 the overall increase of periodicals prices above the
6 general rate of inflation would be with an exigent
7 price change.

8 This particular price change, my
9 understanding is that this will need to be completed
10 by the beginning of October, and I am not sure just
11 when the periodical study will be completed. Once
12 this exigent price change case is closed, periodicals
13 is going to be subject to a price cap with whatever
14 the change in the CPI is.

15 And so this was our opportunity where we
16 felt that we needed to take to make whatever
17 adjustment that we thought we could make.

18 CHAIRMAN GOLDWAY: But there isn't any
19 adjustment for standard and the price cap problem for
20 standard.

21 THE WITNESS: Well, not exactly. Standard
22 mail flats --

23 CHAIRMAN GOLDWAY: They are within a class.

24 THE WITNESS: -- is a product within a
25 class, and so the class as a whole is capped, and so

1 it is possible for us to give above average increases
2 out into the future -- I should say above CPI, and
3 changes out into the future for standard mail flats by
4 just giving more moderate increases to other
5 categories.

6 So this was an opportunity -- and was sort
7 of a unique opportunity to be able to make this change
8 for periodicals. Whereas, we knew that we would have
9 perhaps have other opportunities for standard mail
10 flats.

11 I would also point out that standard mail
12 flats, even with the lower increase, if we look at Mr.
13 Masse's numbers, it actually ends up moving closer to
14 full cost coverage than periodicals with a higher
15 increase.

16 CHAIRMAN GOLDWAY: They start from a
17 different --

18 THE WITNESS: Oh, definitely. They start
19 from a different point.

20 CHAIRMAN GOLDWAY: And I would like to point
21 out for the record that the Commission has been urging
22 the Postal Service to move forward on this periodical
23 study for many, many months, and their portions of the
24 study always seem to be delayed in being produced.

25 So you may not be getting the institutional

1 support that you should to have this available
2 information before making a decision on prices. We
3 would have preferred that that study be completed by
4 now.

5 THE WITNESS: Okay. Thank you.

6 CHAIRMAN GOLDWAY: The next party that has
7 suggested a question is Time Warner, and I will read
8 this. Under your pricing proposal, carrier route
9 flats receive a 9 percent increase, while five digit
10 automated flats receive a 5.8 percent increase. At
11 page 40, lines 9 through 16, you explain that this
12 retains the 9.8 percent rate difference between the
13 two rates, so as not to encourage more carrier route
14 presorting that may be unnecessary in an FFS
15 environment.

16 After the first 100 FFS machines are fully
17 deployed, what percentage of periodical flats will be
18 processed on FFS?

19 THE WITNESS: We have checked with our
20 operations folks, and they told us that their
21 expectation is that if we look at the total flats,
22 periodicals and other flats, that approximately one-
23 quarter to one third of flats would be processed on
24 the FFS after the first 100 machines were deployed.

25 But that they did not have any way to

1 differentiate between periodicals and other flats, so
2 that if we had to pick a number, or a range of
3 numbers, for analyses that we would go with the
4 average of a quarter to a third.

5 CHAIRMAN GOLDWAY: Why didn't the Postal
6 Service elect to establish separate rates for carrier
7 route copies in FFS zones and in non-FFS zones?

8 THE WITNESS: Well, what that was involved
9 with would be a deaveraging of prices, and when we
10 decide to deaverage prices, there are usually certain
11 policy considerations behind it, and one of the
12 effects of deaveraging prices is an effect that we
13 call like the push up-push down effect.

14 And if we had established separate zones, we
15 would have had this push up and push down effect, and
16 given our directive to keep --

17 CHAIRMAN GOLDWAY: Can you explain what the
18 push up-push down effect is?

19 THE WITNESS: Oh, surely. If a certain
20 product -- well, most of our products consist of a
21 range, or perhaps they are all flats, but they may be
22 different kids of flats, or from different sources, or
23 whatever, and different -- or perhaps prepared in
24 different ways, et cetera.

25 So we are not dealing with a totally

1 homogeneous set of mail. So let's say there is a
2 different type of operation, for example. For
3 example, let's pick something like -- well, let's say
4 that we know that standard mail letters is -- well, I
5 should maybe not pick that one.

6 But suppose we had -- well, let's take our
7 parcel post, and right now if you deposit the mail,
8 and it is going to a particular zone, and it weights a
9 certain amount, you pay one price.

10 But that doesn't matter whether you are
11 bringing these pieces, let's say, to a destination
12 facility or not. We do have separate destination
13 discounts, but there is a certain amount of mail that
14 is required, and let's say 50 pieces.

15 If we decided that we wanted to offer
16 separate prices for people who brought, let's say, 10
17 pieces to a BMC, or an NBC now, well, perhaps there
18 are some people who are already doing that. This may
19 be residual mail from a drop ship mail or whatever.

20 What those people who would take advantage
21 of this, or are taking advantage of that, would see
22 their prices fall, and the others, all things being
23 equal, would see their prices go up, because what you
24 are doing is you are deaveraging the price.

25 So that is the push up-push down effect. So

1 when you deaverage, some are going to get higher than
2 they are today, and others are going to get lower, all
3 other things being equal.

4 If we were to set up and to deaverage the
5 carrier route price, we would have had a push up
6 effect that would have gone against the directive that
7 we had to keep the prices for periodicals categories
8 within the close range around the 8 percent, and
9 especially to keep them below a 10 percent increase.
10 So that was one factor that led us not to do that type
11 of deaveraging.

12 CHAIRMAN GOLDWAY: Is that because there is
13 only a quarter of the product that would go to FFS,
14 and three-quarters that would go to a non-FFS zone?

15 THE WITNESS: And also one consideration
16 that we would always make is how much of the mail is
17 this going to affect, and also where -- well, what is
18 the eventual use, let's say, of FFS versus non-FFS.

19 One of the things that we might take into
20 consideration, or that we should take into
21 consideration, is how much of the -- well, the fact
22 that we are in a transition point now, and whether we
23 should be establishing deaveraged prices while we are
24 still sort of in the process of deploying and don't
25 really know how many pieces are going to end up in the

1 FFS zones versus non-FFS zones.

2 CHAIRMAN GOLDWAY: So how do you encourage
3 mailers to use the FFS if there isn't some
4 deaveraging?

5 THE WITNESS: Well, my understanding is that
6 the FFS will be deployed in certain areas, and the
7 mail operation for those areas will be a required
8 preparation. I don't believe that this is going to be
9 an option. The mail will have to be prepared for FFS
10 if it can be used on a machine.

11 CHAIRMAN GOLDWAY: And if they don't get a
12 price rate to do that wouldn't they go to the non-FFS
13 locations?

14 THE WITNESS: Well, the FFS -- the FFS
15 machine will -- is for a sort of particular delivery
16 area. So if mailers want to mail to, let's say,
17 Northern Virginia, and if Northern Virginia is an FFS
18 zone, then they have to give us FFS compatible mail.

19 If they want to reach subscribers or
20 customers in Northern Virginia, this is the kind of
21 mail prep that they are going to need to do. It is
22 not like they can give us mail -- well, do you
23 understand what I am saying?

24 That if it is going to be addressed within
25 an FFS zone, it is going to have to have FFS

1 compatible preparation.

2 CHAIRMAN GOLDWAY: So the drop shipping --
3 the mailers will have to pay for the differentiation
4 in preparation for the FFS zones, and the non-FFS
5 zones, and they will be burdened with additional costs
6 to go to the FFS. So it is sort of deaveraging for
7 them?

8 THE WITNESS: No. We are talking about mail
9 that is being taken to, let's say, a particular place,
10 and mailers are already mailing to Northern Virginia,
11 and let's say that they are drop shopping to that, and
12 they are giving us the mail.

13 CHAIRMAN GOLDWAY: You are going to require
14 them if they are drop shipping in Virginia to prepare
15 the mail to meet FFS standards?

16 THE WITNESS: Well, yeah, but --

17 CHAIRMAN GOLDWAY: But if they are dropping
18 to -- well, I don't know, somewhere in Ohio or Iowa,
19 that doesn't have an FFS?

20 THE WITNESS: They will prepare it
21 differently.

22 CHAIRMAN GOLDWAY: Okay. They will prepare
23 it differently?

24 THE WITNESS: Yes.

25 CHAIRMAN GOLDWAY: So the mailers get the

1 deaverage across, and they are going to have to pay
2 more for one than the other, and there isn't any
3 distinction that you are preparing, the deaveraging?
4 That is the question.

5 THE WITNESS: Well, I want to make sure that
6 I understand the question correctly. What we have is
7 that it is like -- the FFS is like our current DPS
8 system for letters.

9 CHAIRMAN GOLDWAY: The DPS system?

10 THE WITNESS: Yes, the DPS system for
11 letters. If you give us mail -- well, the mail in DPS
12 areas -- well, actually in all areas, and if it is
13 automation mail, it has to be compatible with our DPS
14 machines. In order to get the automation prices --

15 CHAIRMAN GOLDWAY: Was the averaging
16 successful for the DPS?

17 THE WITNESS: I don't -- well --

18 CHAIRMAN GOLDWAY: I mean, there was the
19 averaging that encouraged DPS, and was it successful?

20 THE WITNESS: A very high percentage of our
21 letter mail is now automation compatible, and
22 therefore, DPS'd. I mean, even if it doesn't have the
23 barcode, it is mail that is machinable that we can
24 then put our own barcode on and run through the DPS
25 machines. So there is not a large amount of letter

1 shaped mail that is not machinable left, and on our
2 prices, they reflect that.

3 CHAIRMAN GOLDWAY: Commissioner Langley had
4 a question.

5 COMMISSIONER LANGLEY: I am listening to the
6 discussion and maybe you can help refresh my memory.
7 Wasn't there a requirement that had something to do
8 with labels on periodicals that had to do with --
9 well, the placement of labels on periodicals in order
10 to be FFS compatible, and this required a great deal
11 of discussion between periodical mailers and the
12 Postal Service.

13 And I just don't think there really was a
14 distinction as to whether or not they would -- you
15 know, be able to take advantage of FFS.

16 CHAIRMAN GOLDWAY: That they had to re-
17 engineer the whole front of --

18 COMMISSIONER LANGLEY: Right, they re-
19 engineered everything.

20 CHAIRMAN GOLDWAY: In order to have a
21 different spot for their addresses.

22 COMMISSIONER LANGLEY: Yes, and yet they are
23 not getting the benefit of increased deficiencies. I
24 mean, what is sort of the status of that? And I think
25 it goes in with the general discussion.

1 CHAIRMAN GOLDWAY: Yes.

2 COMMISSIONER LANGLEY: We are looking for
3 efficiencies and --

4 THE WITNESS: Right. An address placement -
5 - and I don't want to get too far beyond my knowledge,
6 but I am aware that address placement on flats is an
7 important component of being able to utilize the FFS.

8 The purpose of the FFS is to hold down flats
9 processing and delivery costs, and to keep them from
10 growing. So to the extent that it keeps down those
11 costs, the mailers do benefit, but they may need to
12 make some changes. For example --

13 COMMISSIONER LANGLEY: Well, they have to
14 make changes.

15 THE WITNESS: Yes.

16 COMMISSIONER LANGLEY: I mean, as the
17 Chairman said --

18 CHAIRMAN GOLDWAY: They have already made
19 changes, and then they will be required to make more
20 changes to prepare their mail, in addition to the
21 address for FFS. But only 25 percent of that mail is
22 going to be -- have the opportunity to use FFS.

23 THE WITNESS: Yes. Well, this number, the
24 one-quarter to one-third, refers to the amount of
25 estimated coverage from the first wave of deployment.

1 I don't think we are claiming that only 25 percent of
2 the flats mailed will ever be able to get any benefits
3 from this.

4 I mean, to the extent that it holds down the
5 costs of our products, all mailers who use those
6 products will benefit. It doesn't necessarily require
7 that every change that improves or increases our
8 efficiency be given with a discount.

9 And in this particular case, we know that
10 the periodicals and the standard mail flats are
11 struggling to cover costs. So to the extent that we
12 have efficiencies gained through FFS, that would mean
13 that the amount that we would have to increase prices,
14 and not necessarily where we would end up lowering
15 prices, but the amount that we would have to increase
16 prices would be smaller.

17 So as I think I pointed out in some of the
18 discussion earlier today, that the cost coverage
19 really is the result of an interaction between costs
20 and the revenues, or the prices. So to the extent
21 that we can gain efficiencies through costs, that
22 means that we have to rely less on price increases to
23 move these towards full cost coverage.

24 CHAIRMAN GOLDWAY: There is another question
25 here from Time Warner. It points to the annual

1 compliance determination reports that we issued in
2 2009, and I will quote from that.

3 "The low pass throughs are problematic for
4 two reasons. First, they exacerbate the periodicals'
5 cost to revenue gap, because mailers are not paying
6 for the full cost of handling bundles and containers."

7 "Second, the combination of low and
8 differential pass throughs may send conflicting price
9 signals to mailers, and prevent them from entering
10 mail in a way that reduces the end-to-end costs.
11 Current opportunities exist to improve efficiency and
12 to offer mailers appropriate pricing incentives. The
13 Postal Service should implement such changes as soon
14 as practicable."

15 In your statement, you say that in light of
16 these considerations the Postal Service believes that
17 an above-average increase of 8 percent, together with
18 a plan of gradual improvement of cost coverage,
19 represents a judicious balance between quickly
20 resolving the periodicals cost coverage problem and
21 ensuring the best prospects for the long term health
22 of the periodicals industry.

23 The question is can you clarify what you
24 mean by a plan of gradual improvement of costs
25 coverage?

1 THE WITNESS: Well, I think that can be
2 taken at its face value. The words can be taken at
3 face value. What we are trying to do is we are trying
4 to pay attention to the possibilities for enjoying a
5 cost savings, to the extent that we can get some of
6 them from some of the initiatives in the flats
7 initiatives, the flats strategy. We will gain those.

8 We also are going to monitor, for example,
9 the effects of economic recovery, and to see if this
10 can sort of help periodicals. We note and I have been
11 told that there is some improvement in advertising
12 pages, and this maybe needs some improvement in weight
13 in some recent data that we have seen.

14 That has the potential for improving the
15 situation for revenues for periodicals, even aside
16 from our price increases. We are offering, and we are
17 asking for a price increase here of eight percent.

18 And we will use pricing to help as one of
19 the parts to fill in the gap. We realize that this is
20 not something that can be solved overnight.

21 CHAIRMAN GOLDWAY: You don't have a time
22 frame?

23 THE WITNESS: We do not.

24 CHAIRMAN GOLDWAY: Gradual improvement means
25 what?

1 THE WITNESS: Well, it means that we are
2 going to try to move this along as quickly as we can,
3 and within the kind of -- in terms of pricing, it
4 means we will try to move on as quickly as we can
5 within the restrictions that are on us with respect to
6 price changes.

7 And we are also going to be looking for
8 efficiencies, and we note that in the Commission
9 statement, in the annual compliance determination, the
10 Commission stated that they believed that there were
11 some -- they expressed some concern with some of the
12 pass throughs for some of the container based pricing.

13 CHAIRMAN GOLDWAY: That's right.

14 THE WITNESS: Yes, and that the Postal
15 Service agrees that there are opportunities there
16 for --

17 CHAIRMAN GOLDWAY: So does your plan for
18 gradual improvement include bringing bundle and
19 container price cost ratios close to a hundred percent
20 as soon as practicable?

21 THE WITNESS: Well, it was a gradual step of
22 moving them closer to a hundred percent, and yes, as
23 soon as practicable, taking into consideration the
24 fact that we will be looking at what some of these
25 particular changes may have, and whether they -- you

1 see, we make changes in certain price elements.

2 We have to be aware of the impacts, and
3 sometimes the impacts can be spread broadly, and
4 sometimes the impacts are more focused, and they
5 affect certain segments of an industry more than
6 others, and that is a consideration that we would want
7 to take.

8 So we are going to be trying to move as
9 quickly as we can without sort of overturning the
10 apple cart.

11 CHAIRMAN GOLDWAY: If we did get cost
12 coverages that were close to -- or pass throughs that
13 were close to 100 percent, how much would that improve
14 the price cost ratios for periodicals?

15 THE WITNESS: Well, I have been told that --
16 well, are you talking about work share, and all of the
17 discounts, the ones that exceeded avoided costs?

18 CHAIRMAN GOLDWAY: Yes.

19 THE WITNESS: Okay.

20 CHAIRMAN GOLDWAY: I believe there are nine
21 of them.

22 THE WITNESS: Yes. We are talking about the
23 same things, and not necessarily about the cost pass
24 throughs, for like bundles or something. I have been
25 informed that bringing these close to a hundred

1 percent would have a positive effect, but a rather
2 small one.

3 CHAIRMAN GOLDWAY: How much?

4 THE WITNESS: I have seen figures that are
5 in a single digit millions of dollars, as compared
6 with overall periodicals revenue of about \$2 billion.
7 So it is small. It is positive, but small.

8 CHAIRMAN GOLDWAY: And how far would price
9 cost ratios of bundles and sacks help?

10 THE WITNESS: I don't have a quantification
11 of that. I do note that we are moving some of those
12 in the direction. One of the -- well, I'm sorry, but
13 you said bundles and sacks, and that doesn't focus on
14 the pallets.

15 One of the effects, or one of the outliers
16 in our periodicals price changes was that we did
17 actually give a fairly significant increase for origin
18 pallets, and so that has a way of moving that.

19 We are also going to be moving other
20 containers and periodicals in the direction of trying
21 to increase the recognition of costs in the price. We
22 have a ways to go. We have made some --

23 CHAIRMAN GOLDWAY: Okay. Throw in pallets,
24 too. What would be --

25 THE WITNESS: I don't have a figure on that.

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CHAIRMAN GOLDWAY: Can you get it for us?

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THE WITNESS: I will pass that along to some of the folks. I don't know how easy or how difficult that will be to provide an estimate, but I will pass that along.

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CHAIRMAN GOLDWAY: Please try and get that information for us and report back. And while you are at it, do you have a guess as to how many years you are talking about when we are talking about a gradual process of getting --

THE WITNESS: Well --

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CHAIRMAN GOLDWAY: I know that you have been very vague here. Do we have a reference? Two years, four years, or 10 years until we get out to the end of the envisioning of the future? What do you think?

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THE WITNESS: One of the things that I took away from Commissioner Acton's discussion with me right before the break was how difficult it is to predict what might happen in the future. It would be -- I don't actually have a number of years. I can't --

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CHAIRMAN GOLDWAY: One of the things that Commissioner Acton was pointing out is that we have a regulatory responsibility to assure that the pass

1 throughs are no greater than 100 percent.

2 THE WITNESS: Absolutely. I understanding.

3 CHAIRMAN GOLDWAY: That the Postal Service's
4 pricing is efficient and fair, and I don't know how
5 long we are going to be able to wait.

6 THE WITNESS: Understood, but I would hope
7 that the Commission would look and see that we are
8 making progress, and give us credit for making
9 progress. I mean, if you look at Mr. Masse's
10 attachments, you see that we actually have made
11 significant progress.

12 And if we look at a full years
13 implementation for periodicals, I think we are up to
14 around 87 percent cost coverage, which we are
15 hopeful -- I think we all hope for a variety of
16 reasons that the economy will improve.

17 But how long it is going to take, it is
18 difficult to say. There are many conditions that
19 factor in our ability to raise prices, and the ability
20 of various customers of ours to absorb price
21 increases.

22 And how much they will be able to improve
23 just through the general improvement in economic
24 conditions. There are so many things out there. What
25 I would hope that the Commission would do is take a

1 look and see if we are making progress.

2 And perhaps as the economic picture becomes
3 clearer, we may be able to come up with more
4 definitive numbers, but I think somebody earlier
5 mentioned -- I thought someone had mentioned double
6 dip recession, and we don't know what is going to
7 happen.

8 CHAIRMAN GOLDWAY: Within the price
9 structure that you have presented which presort levels
10 of periodicals and standard flats are given incentive
11 to migrate to FFS so that they would eventually
12 benefit from this new efficiency?

13 THE WITNESS: There aren't any price
14 incentives to migrate to FFS. FFS is going to be --
15 once FFS is deployed in an area, it is my
16 understanding that that is going to be the -- well, in
17 order to get the automation prices, that is going to
18 be the preparation that is going to be required.

19 So it is not like -- this is not like a
20 choice between presorting to three digits or five
21 digits. It is preparation that if you want to get our
22 automation prices in a particular area, you are going
23 to have to use this particular preparation.

24 Not that these preparations are especially
25 erroneous. In fact, it may be that they will be less

1 difficult. I mean, when I am talking about the actual
2 preparation, in terms of how the mail is presented,
3 and not whether they will -- well, things like address
4 placement.

5 COMMISSIONER LANGLEY: Are you talking about
6 the costs to the mailer as not being erroneous? Like
7 the re-engineering label plate?

8 THE WITNESS: No, I was talking about that
9 once that process is done, I was talking about --
10 well, you see, I understand that the Postal Service
11 is publishing some new rules that allow mailers to
12 enter mail prepared for FFS, where they don't have to
13 make the small bundles anymore.

14 They can give us larger bundles that are set
15 up for the FFS schemes now. So that would in fact
16 ease the preparation burden on that for actually
17 preparing mail, and this is a separate issue from
18 address placement. I mean, that is something that is
19 needed, because otherwise FFS is not going to work.

20 CHAIRMAN GOLDWAY: Okay. I am going to
21 yield to Commissioner Acton for questions.

22 COMMISSIONER ACTON: Thank you, Madam
23 Chairman. There is a handful of questions that I have
24 on improvements.

25 THE WITNESS: Sure. Are we talking about

1 operational efficiencies?

2 COMMISSIONER ACTON: No, we are willing to
3 discuss any aspect of this improvement that you are
4 willing to talk about, but let me just cite for you
5 the portion of the ACD that I am referring to.

6 THE WITNESS: Okay. Yes, please.

7 COMMISSIONER ACTON: We make a note that
8 opportunities exist to improve efficiency and to offer
9 mailers appropriate pricing incentives, and we
10 encourage the Postal Service to implement such
11 strategies -- I'm sorry, such changes as soon as
12 practicable.

13 THE WITNESS: Yes. Okay. In that
14 particular quote, it is about pricing, using pricing
15 as an incentive to get more appropriate mailer
16 behavior. Well, we expect that each time we change
17 the prices, we expect to try to move in the
18 appropriate direction.

19 We think that there are opportunities, such
20 as trying to reflect more of the container costs at
21 the various container levels in the prices, and we
22 expect that these will be reflected in our subsequent
23 price changes.

24 COMMISSIONER ACTON: So you can see that
25 what encourages us a lot when we had these

1 interactions with you, and for instance, with your
2 predecessor here this morning, Mr. Neri, is that when
3 we have some definitive sort of information about time
4 frames -- and, for instance, at the closing of Mr.
5 Neri's discussion, he indicated that come August that
6 there will be a critical path assessment for some
7 important productivity measures which we are looking
8 forward to having.

9 THE WITNESS: Well, as I said, we expect to
10 take steps -- well, under the PAEA, we now engage in
11 fairly regular price changes, and in those price
12 changes, we expect to be moving these prices in a way
13 that should encourage efficiencies.

14 So this is -- well, I don't think that the
15 Postal Service can commit to, let's say, going to a
16 hundred percent cost coverage the next time we change
17 prices.

18 COMMISSIONER ACTON: Don't misunderstand me.
19 I don't believe that we are talking you to make that
20 type of commitment. What we would like you to commit
21 to do is to develop a time frame, a tentative time
22 frame for us to look at some aspects, so that we can
23 better understand how quickly you may be planning as
24 an organization to address these recurring problems.

25 Let me just ask. Have you developed any

1 benchmarks that you may be using to measure your
2 success in implementing these types of change?

3 THE WITNESS: Are we talking specifically
4 about --

5 CHAIRMAN GOLDWAY: Pricing incentives.

6 THE WITNESS: Well, pricing incentives, for
7 example, such as the ones that were requested in the
8 ACD. I am not aware of those, but I would have to
9 check with --

10 COMMISSIONER ACTON: Well, I think what we
11 are focusing on are efficiency in pricing benchmarks.
12 Some sort of meaningful milestones which we can look
13 to, to understand what sort of detailed progress we
14 are making.

15 CHAIRMAN GOLDWAY: I think for your own
16 management, it seems to me that you should be saying,
17 okay, we are going to try and address 25 percent of
18 this problem every year for the next four years, or 30
19 percent of the problem for the next three years.

20 THE WITNESS: Understood.

21 CHAIRMAN GOLDWAY: Or some sort of
22 quantifiable, relatively reasonable, accomplishable
23 goal.

24 THE WITNESS: Well, I think that last word
25 is a key element, and perhaps one of the things that

1 makes it difficult to
2 -- let's say address some of the periodicals problems
3 through pricing is that periodicals as a class is
4 price capped, and that restricts the amount of price
5 changes that we can make on an annual basis.

6 And we don't know the change, and to say
7 that we can -- for example, let's look at Mr. Masse's
8 estimate that if we had a full year of the new prices
9 for periodicals that we think that we would end up
10 covering under the assumptions -- you know, the
11 economic assumptions, and we would cover about 87 or
12 so percent of our costs.

13 To say that we would be able to eliminate
14 that over the next three years, we are talking 12-1/2
15 percent or 13 percent, and would require a significant
16 change. If it were to all fall on pricing, it is not
17 clear that we would have the capability, and it would
18 be achievable to increase periodicals prices as 3 or 4
19 percent a year if inflation turns out to be 1 or 2
20 percent a year.

21 CHAIRMAN GOLDWAY: Couldn't you commit to a
22 combination of pricing and efficiency gains, because
23 apparently Mr. Neri doesn't have any benchmarks either
24 in terms of efficiency gains for the --

25 THE WITNESS: Well, I understand your

1 frustration with that, and the postal service really
2 is concerned about this, and if we were to give -- you
3 know, let's say two percent a year, because that
4 happens to be the inflation rate for the next 3 or 4
5 years, we still wouldn't get there. We would need to
6 get more from efficiency improvements.

7 We are going to try to do our best, and I
8 realize that that is a challenge for us to do, and for
9 you to rely on, but we have to try to use sort of both
10 blades of the scissors. I mean, they have to work
11 together.

12 COMMISSIONER ACTON: We are not trying to
13 discourage you.

14 THE WITNESS: No, I understand that.

15 COMMISSIONER ACTON: I think we have made
16 our point. We are just trying to understand what your
17 proposal may be for how you are going to approach this
18 going forward.

19 THE WITNESS: We will try to capture all
20 efficiencies, operational efficiencies that we can,
21 that through the analysis process that if we invest in
22 some of these efficiency measures that we are
23 discussing, that Mr. Neri discussed, we ought to make
24 sure that they actually gain something close to what
25 we are expecting to make the payoff worth the

1 investment.

2 We don't want to find ourselves even further
3 in the hole than we were. So all of those have to be
4 put through their analysis, and they will give us some
5 of the -- sort of one-half of the equation, and the
6 other half, we will have to see what we can do with
7 pricing.

8 But at this time, I don't have projections
9 for cost savings, and I don't have or I don't know
10 that we can commit to a specific timetable. We will
11 try to increase prices in a way that utilizes our
12 legal capacity to do so as long as we don't feel that
13 we are doing it in a way that is going to cause damage
14 to our customer base.

15 COMMISSIONER BLAIR: Dr. Kiefer, I am
16 sensing from you from what you have been saying today
17 that there is a general frustration -- and I don't
18 know if you are reflecting the Postal Service's
19 frustration with the price cap mechanism.

20 THE WITNESS: Well, I think that -- well, I
21 am not sure that I can -- I don't know how far I
22 should go in speaking for the Postal Service on this,
23 but I should point out that the price cap mechanism
24 applied at the class level enables us to handle
25 situations.

1 For example, like standard mail flats, where
2 it is a portion of a class that is not covering its
3 costs, and we have opportunities to move along, but
4 stay within the cap, but the current system poses some
5 significant challenges to the Postal Service.

6 And I think we all feel that frustration
7 that the only -- well, the only mechanism that I know
8 of to break through the cap is the exigent price
9 change, and it doesn't handle the situation where a
10 whole class is not covering its costs.

11 I mean, it is applied at the class level,
12 and so we can only increase the price of periodicals
13 outside of an exigent price change at the regular CPI
14 rate.

15 COMMISSIONER BLAIR: So would it be fair to
16 say that if Congress had not passed the PAEA in 2006
17 that periodicals rates would be significantly higher
18 today than they would have been otherwise?

19 THE WITNESS: Well, that may be more than I
20 could say, but there is a requirement that if Congress
21 had not passed the PAEA, and we were under the former
22 regime, the PRA regime, that had a requirement that
23 some classes of mail would cover their costs, and they
24 would have increases as large as was required to cover
25 the costs.

1 Now, here has been several price changes and
2 other situations going on between that. I am not sure
3 how everything would have played out, but we would
4 have been required to propose prices that cover the
5 costs. I mean, that is just part of the way the law
6 went. So I think that certainly is possible, that
7 prices would have been higher.

8 COMMISSIONER BLAIR: And I think that is
9 probably one of the reasons that Congress passed the
10 PAEA and the price cap mechanism must have kept rates
11 down, and it caused the Postal Service to make
12 efficiencies, and cut costs.

13 THE WITNESS: That is clear, but I wanted to
14 couch my answer, or make clear that my answer was
15 referring mainly in the periodicals area, because we
16 would have been required to cover those costs.

17 If we had not had the PAEA passed, the old
18 subclasses, which were larger aggregations, would
19 still have been in existence, and we perhaps would not
20 have been dealing with the issue of standard mail
21 flats in the same way that we are dealing with it
22 today.

23 COMMISSIONER BLAIR: You have been quite
24 generous in your in your answers, and I know that it
25 is getting late, but I just hear a yearning for the

1 previous system, and I just wanted to see if you could
2 clarify that.

3 THE WITNESS: No, I am certainly not
4 expressing the view of the Postal Service in saying
5 that we would rather go back. I mean, I have no -- it
6 is not my call, and even as a professional pricer, it
7 is a much more complex issue.

8 But there is no system that is perfect, and
9 I think we are still fairly young in the life of the
10 PAEA system, and I think we have found out fairly
11 early on some of the difficulties, and that is what I
12 wanted to illustrate, and not to damn the whole
13 system.

14 But we recognize that we have
15 not found a good way to deal with the situation where
16 we know we need to adjust prices for a class, and we
17 are limited by a price cap.

18 CHAIRMAN GOLDWAY: It is a dilemma.

19 THE WITNESS: Absolutely.

20 CHAIRMAN GOLDWAY: And that efficiency gains
21 are meant to address.

22 THE WITNESS: Yes.

23 CHAIRMAN GOLDWAY: With regard to the PAEA,
24 the PAEA does give the Postal Service great
25 flexibility with regard to pricing for competitive

1 products, and in your testimony on page 11, you say
2 that for purposes of developing prices for this
3 request, we have used planning assumptions concerning
4 the prices for certain competitive products that will
5 take effect in January of 2011.

6 Could you discuss the basic feature of these
7 assumptions and explain how they were applied to
8 periodicals, or to other market dominant products?

9 THE WITNESS: I am not sure that this was --
10 that this really applied to periodicals, but I can
11 give you an example in -- for example, in --

12 CHAIRMAN GOLDWAY: We weren't sure. What
13 does it apply to?

14 THE WITNESS: Well, okay, here is a very
15 precise example. In standard mail certain residual
16 pieces -- and because there is no single piece price
17 for standard mail, but certain residual pieces must
18 pay either first-class prices, or if they weigh more
19 than the upper limit for first-class, they pay
20 priority mail prices.

21 Priority mail, of course, is a competitive
22 product. So in order to estimate what the overall
23 effect of our price change was, we needed to look at
24 what the price change would be for priority mail to
25 estimate what would be the effect on this rather small

1 segment of standard mail.

2 I believe that for the purposes of that
3 estimate, we put it at a number like -- I think we put
4 in five percent, which is sort of the mid-range of our
5 market dominant. I mean, that is not to say that
6 priority mail on average is going to go up by five
7 percent, but we use that as a planning assumption.

8 That is the purpose of this portion of my
9 statement. It did not refer to periodicals. I am not
10 aware that the two are that connected to periodicals.

11 CHAIRMAN GOLDWAY: Any other questions?

12 COMMISSIONER ACTON: Did you want to
13 complete the sheet?

14 CHAIRMAN GOLDWAY: I think we can move on to
15 standard.

16 THE WITNESS: All right.

17 CHAIRMAN GOLDWAY: And try and get through
18 some of these before we take a break.

19 THE WITNESS: Surely.

20 CHAIRMAN GOLDWAY: With standard mail, I
21 will begin with some of the questions referred to by
22 our participants. The Greeting Card Association
23 points to your statement where you use the phrase
24 "full coverage".

25 They have questions about its meaning as to

1 "we". On page 7, lines 14 to 15 of your statement,
2 what is meant by the phrase "gradually moving to full
3 coverage"?

4 THE WITNESS: In general, when I use the
5 term "full coverage", it meant that we would cover our
6 attributable costs.

7 CHAIRMAN GOLDWAY: Does full coverage mean -
8 - do you mean the system-wide average cost coverage,
9 or just a hundred percent of attributable costs?

10 THE WITNESS: When I applied that -- I'm
11 sorry, when I used the term, I believe I was talking
12 about individual products, or classes of mail, and
13 that meant that they would fully cover at least a
14 hundred percent of their attributable costs.

15 CHAIRMAN GOLDWAY: Now, the Greeting Cards
16 Association asked for a timeline as to gradually move
17 to full coverage, but I am afraid to ask the question.

18 THE WITNESS: Yes.

19 CHAIRMAN GOLDWAY: I think we have covered
20 the issue of whether we are going to have any fully
21 accountable, quantifiable timeline from the Postal
22 Service, at least from your answers in the negative.

23 The next question is from Valpak, and their
24 question is the price increase for standard flats is
25 below the 5.6 percent average. It is 5.1 percent.

1 Why do you believe that incurring continued
2 substantial losses is reasonable and equitable for the
3 Postal Service, particularly when other mailers are
4 required to pay higher coverages to offset these
5 losses?

6 THE WITNESS: Well, under the -- if we were
7 required to reach a breakeven or a particular level of
8 revenue, I would say that the other mailers might be
9 required to sort of make up the difference, but at
10 this point we're overall we're losing money. So I'm
11 not sure I agree with that part of the statement. But
12 I want to address the question that sort of it's
13 behind that.

14 I want to point out first of all that
15 standard mail flats, which is a major one of our
16 products that is being used, you know, large part by
17 the catalog industry, is being given a significant
18 increase, you know, 5.1 percent. This is not higher
19 than the average but it was, the Postal Service is
20 concerned that this is, the catalog industry is in a
21 delicate position. It has had to withstand the
22 effects of the economic recession, retail sales are
23 down, that's one of those driving factors that affect
24 the catalog business.

25 We're concerned that raising the prices very

1 rapidly or in large steps on, for this particular
2 product, might cause significant harm to the hard copy
3 mail catalog industry. There is an electronic
4 alternative to this. We believe though that there is
5 great value in catalog mail, and we also believe that
6 as a whole, taken as a whole, that catalog mail, this
7 catalog industry, is a profitable industry for us.

8 We definitely want to move standard mail
9 flats toward full cost coverage, but we do not want to
10 take steps that might cause catalog mailers to trim
11 their mailing lists or get out of the hard copy mail
12 system altogether. There are other mail products that
13 these catalog mailers use which contribute, make
14 positive contributions. And we think that on the
15 whole we're making money on this industry and we don't
16 want to take steps that's going to drive it away.

17 CHAIRMAN GOLDWAY: Do you have any
18 statistical information, any data, to show the
19 relationship between catalogers and the other parts of
20 the mail stream that they use that would in any way
21 indicate that the, that industry provides at least a
22 breakeven for you, if not a profit as you suggest?

23 THE WITNESS: The Commission asked POIR
24 number 3 question 7, asked about this, and I checked
25 with our product management folks and they provided

1 some information which is actually submitted in public
2 form in response to this, and we actually I think sent
3 a nonpublic version, that shows the usage of the top
4 600 catalog mailers in the various products. Before
5 this hearing began we were approached and asked about
6 one of the labels on the --

7 CHAIRMAN GOLDWAY: Right.

8 THE WITNESS: Commissioner, do you have
9 this?

10 CHAIRMAN GOLDWAY: Yes, and --

11 THE WITNESS: You have it available?

12 CHAIRMAN GOLDWAY: There was a confusion
13 about --

14 THE WITNESS: Yeah, there was a confusion, I
15 apologize for that confusion. We have been pretty
16 busy lately and sometimes things slip through the
17 cracks. We have contacted those who are familiar with
18 this analysis and I can confirm that the data, like
19 the revenue and volume data in this table, are for
20 Fiscal Year 2009. So that the label, the first line
21 label where it says, it says Q2 FY 2010, that is
22 erroneous. That is, these data here are for 2009,
23 Fiscal Year 2009.

24 If you look at the top line there, these
25 estimates suggest that we are more than covering our

1 costs from these catalogers. So the Postal Service
2 does believe that this is a, although it's a
3 vulnerable segment of our business, the customers are
4 vulnerable, and we want to move gradually toward full
5 cost coverage, we note that they're users of a broad
6 range of products. Standard mail flats is not
7 covering its costs, we think it should.

8 We think we have the opportunity to as the
9 economy improves and the catalog industry is more able
10 to withstand more increases in this particular product
11 that we can move toward adjustments. And we also hope
12 that some of the flat strategy initiatives will give
13 us that sort of that other branch of the equation, you
14 know, so that we can get some efficiencies on one hand
15 and on the other make appropriate price adjustments.

16 But we think this is a profitable segment of
17 our business and we're reluctant to try to push it all
18 the way, push this particular product all the way to
19 100 percent because we know it, we're aware of the
20 fact that it could be seriously damaged, that catalog
21 mailers will trim their lists or maybe even just give
22 up on paper catalogs.

23 CHAIRMAN GOLDWAY: My staff tells me they're
24 going to be asking more questions about this --

25 THE WITNESS: Okay.

1 CHAIRMAN GOLDWAY: Document that you've
2 submitted now that they have a better understanding of
3 what the headings are.

4 THE WITNESS: Surely.

5 CHAIRMAN GOLDWAY: But one of the questions
6 that they had was sort of related to this was that,
7 you've stated that it's believed the Postal Service
8 has only a small percentage of the total of
9 fulfillment shipments from catalogs, catalogers?

10 THE WITNESS: Yes.

11 CHAIRMAN GOLDWAY: Aren't you concerned that
12 you're providing this special consideration to
13 catalogers and not getting any commitment in return
14 from them?

15 THE WITNESS: Well, I think there are
16 opportunities for sort of contractual arrangements, I
17 mean like NSAs or other types of arrangements where we
18 can sort of have a, we can make arrangements for if we
19 give you sort of a contract pricing that you would
20 agree to use our shipping products. At this point I'm
21 not aware of any, I'm pretty sure there wasn't any
22 kind of quid pro quo in doing this. I note that the
23 Catalog Mailers Association has joined with other
24 parties in opposing this particular -- we're trying to
25 do what we think is best for the catalog industry, and

1 so --

2 CHAIRMAN GOLDWAY: I believe it was
3 Commissioner Langley who pointed out that that kind of
4 an NSA would be a very good opportunity and we've been
5 disappointed that we haven't seen that kind of NSA
6 from the Postal Service. So you can take back our --

7 THE WITNESS: We'll take your concerns.

8 CHAIRMAN GOLDWAY: Our comments that we're
9 interested in that. And then one other question
10 before I offer my Commissioners other opportunities.
11 You know, the periodical mailers tell us the same
12 thing, that if you add up the first class mail that
13 they, and the standard mail that they include in the
14 system for billing and for advertising and for
15 communications and for special packages that are part
16 of a subscription, that their products also would more
17 or less cover costs. Have you done any research with
18 regard to the periodicals mailers?

19 THE WITNESS: I'm not sure that, I
20 personally haven't done it, I'm not sure whether
21 something like this has been done. I believe in
22 response to one of these questions we did send along
23 some information that indicated, I believe it was some
24 usage by periodicals of other portions of mail.
25 Commissioner, before lunch Commissioner Hammond, I

1 believe it was, asked the question whether we ever
2 were trying to develop let's say prices or other
3 programs to get rid of customers. The answer is
4 absolutely not.

5 We value our customers in the catalog
6 industry, we value our customers in the periodicals
7 industry. And as I said in response to that, we look
8 to the long term, and we think that all of these
9 products, that the periodicals products and others can
10 be profitable to us. We are at the same time we are
11 constrained, you know, by some of the goals and
12 factors of the PAEA to try to ensure that periodicals
13 cover their costs.

14 So we're always in a balancing situation.
15 We hear from the Commission and we've heard it, we've
16 seen it in the ACDs, I'm hearing it today, there's
17 very great concern about our products that are not
18 covering our costs. We also are thinking that we want
19 to retain these. I mean I'm not sure whether if
20 somebody told me to come up with a plan to get rid of
21 unprofitable mail or to get rid of a lot of mail that
22 was not, whether just jacking up the prices wouldn't
23 be the best answer. We're not trying to get rid of
24 mail, we think mail can be profitable, we want to make
25 it cover its costs, but we're not going to try to lose

1 it by making it prohibitively expensive or making the
2 cost increases too hard to swallow.

3 CHAIRMAN GOLDWAY: Commissioner Acton?

4 COMMISSIONER ACTON: Dr. Kiefer, in your
5 response to the presiding officer's information
6 request number 3 question 8 --

7 THE WITNESS: Question 8.

8 COMMISSIONER ACTON: You indicated "The
9 Postal Service has not yet been able to produce home
10 price elasticity estimates for standard mail flats"?

11 THE WITNESS: That's correct.

12 COMMISSIONER ACTON: And we'd like to know
13 if the Service has endeavored to produce these
14 estimates, and if so what types of challenges have you
15 encountered and why have you been unable to produce
16 those home price elasticity numbers?

17 THE WITNESS: This is not my area of
18 expertise, but I can report to you that our
19 forecasting people have made attempts to do that. One
20 of the challenges that they face is that the kind of
21 information that they need, they don't have, in their
22 view they don't have sufficiently long time series to
23 be able to do that.

24 Standard mail flats is a relatively,
25 although we have had standard mail flats and standard

1 mail for quite some time, the kind of data that they
2 feel they need has only been available for a
3 relatively shorter period of time. I think it, I have
4 asked about this and I believe response I get is that
5 it will be a little while, maybe several more years,
6 before they feel that they will have enough data to be
7 able to produce demand equations with sufficient
8 significant values, statistically significant values,
9 to be able to use.

10 COMMISSIONER ACTON: Okay. I think we can
11 move to package services, right?

12 CHAIRMAN GOLDWAY: Well, I just, I don't
13 want to get into a long discussion about this because
14 we did a long discussion about this issue with regard
15 to periodicals.

16 THE WITNESS: Yes.

17 CHAIRMAN GOLDWAY: But I do want to point
18 out, and staff has, that in our ACD the Commission has
19 asked the Postal Service to devise a plan to improve
20 the cost coverage of standard mail flats products and
21 to narrow the differences between standard mail
22 letters and standard mail flats. And you have
23 indicated that unlike periodicals standard mail flats
24 and letters are within a general class and there is an
25 opportunity over time to make adjustments to respond

1 to the concerns that we've articulated in the annual
2 compliance determination.

3 THE WITNESS: Right, right.

4 CHAIRMAN GOLDWAY: So my question is, is
5 there a time line for the Postal Service to achieve
6 the goals that the Postal Regulatory Commission has
7 directed you to achieve?

8 THE WITNESS: Okay. Again I don't have a
9 time line, although certainly I think it would be
10 clear that given the urgency of moving standard mail
11 flats to full cost coverage we would be giving, it
12 would be likely that provided that we felt confident
13 that the types of price changes that we were giving
14 would not be damaging that we would be ready to give
15 above average increases to that. Now given that
16 standard mail, letters and flats are pretty much
17 exhaust standard mail, the only way you can give a
18 above average increase to standard mail flats would be
19 giving a below average increase to the letters.

20 I would point out, and I don't want to make
21 too big of a deal about this, but if you turn to page
22 28 of my statement and you see that the various
23 categories, that standard mail flats in this
24 particular case is actually given a slightly higher
25 percentage increase than standard mail letters. It's

1 a minimal amount, but it's, we take seriously the
2 concerns expressed by the Commission.

3 CHAIRMAN GOLDWAY: What I would like from
4 you is, if it's at all possible, is some specific
5 answer with regard to standard mail flats and letters
6 that addresses the concerns raised in the annual
7 compliance determination and gives us some idea of a
8 time line that includes both cost efficiencies and
9 prices. We didn't get very much information from Mr.
10 Neri and we're not getting very much information from
11 you, and this concern of ours goes well beyond the
12 exigency case to the heart of the regulatory process.
13 But I'm taking this opportunity to ask you to provide
14 a document for us that gives us some indication that
15 you're looking at the nexus of cost savings and
16 pricing and that you have a commitment that's
17 measurable to addressing those concerns in the next
18 few years, two or three years.

19 COMMISSIONER ACTON: It could be something
20 to keep in mind, Dr. Kiefer, when you're preparing
21 your annual compliance report, since you are being --
22 you talked earlier about what the Service should
23 deserve credit for and what you certainly deserve
24 credit for, and we had this discussion in board rooms
25 when we were looking over this proposal, and that is

1 that regardless of your particular approach in this
2 particular request, you are understanding our concerns
3 that we outlined in the annual compliance
4 determination --

5 CHAIRMAN GOLDWAY: Yes, that's true.

6 COMMISSIONER ACTON: And you're making some
7 movement in most instances to try to resolve it. I'm
8 not saying that the movement you're making is what we
9 would endorse. What we're looking for is a little
10 more information of the type that the Chairman's
11 describing because that would give us a little more,
12 in fact quite a lot more, enlightenment about whether
13 or not what you're proposing is something that we can
14 approve.

15 THE WITNESS: I hear you, and we will send
16 you something.

17 CHAIRMAN GOLDWAY: Okay, with that I think
18 we've completed standard mail. And our next topic
19 would be package services. But I think we'll take a
20 break for 15 minutes and come back. I think package
21 services and special services should take less time,
22 and hopefully we'll be out of here by 4:30, that's my
23 goal.

24 THE WITNESS: I hope so.

25 CHAIRMAN GOLDWAY: Okay, see you in 15

1 minutes.

2 (Whereupon, a brief recess was taken.)

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1 CHAIRMAN GOLDWAY: We're reconvening.
2 Unless any of my colleagues tell me differently I
3 think there's only one question regarding package
4 services, is that right? And it involves the
5 relationship between low weight parcel post and
6 priority mail. The Postal Service proposes to allow
7 prices for low weight parcel post to vary by zone for
8 the first time, leading to parcel post rates that are
9 higher than retail priority mail counterparts.

10 THE WITNESS: Yes.

11 CHAIRMAN GOLDWAY: On page 64 of your
12 testimony you state that the constraint that parcel
13 post rates must be lower than unzoned priority mail
14 rates is "no longer relevant". Does the Postal
15 Service intend to keep low weight priority mail rates
16 below corresponding parcel post rates? And is this an
17 appropriate price signal to send to mailers?

18 THE WITNESS: The situation is really boils
19 down to one of timing. As I mentioned, and I believe
20 you referred to this earlier, that we, when we were
21 developing prices, we have not yet finalized the
22 prices for our competitive products, and that includes
23 priority mail. So the prices that we are proposing
24 for single piece parcel post, in a few price cells, in
25 the 1 and 2-pound area, they do exceed the current

1 prices for retail priority mail. As I indicated, I
2 believe it was on page 11 of my statement, we will be
3 adjusting competitive prices, and my understanding is
4 that when the priority mail prices are adjusted these
5 cells, the priority mail prices in these cells will
6 not be below the single piece parcel post prices.

7 CHAIRMAN GOLDWAY: So you do think that in
8 principle having the parcel post prices lower than
9 priority mail prices is the appropriate structure?

10 THE WITNESS: Well, I am, in general I
11 personally think that it's good to have -- well I
12 think they shouldn't be above. I mean I don't know
13 whether the people who price the competitive products
14 -- I realize that we're talking about the one zone
15 that is still -- I shouldn't say zone. I don't know
16 whether, well I would not be the one to rule out their
17 pricing them in certain cells at the same price. So
18 I'm just saying they will, I understand they will not
19 price priority mail below parcel post. So I can't,
20 the prices have not been finalized, my --

21 CHAIRMAN GOLDWAY: Since the service for
22 parcel post is less than the service for priority
23 mail, it seems to me that that is not a logical
24 pricing strategy to offer to customers.

25 THE WITNESS: Well, I will convey that --

1 CHAIRMAN GOLDWAY: But you're assuring me
2 that at least in the short run for this particular
3 proposal you're making that you believe priority mail
4 prices will not be lower than parcel post. You're not
5 assuring me that they'll be higher?

6 THE WITNESS: Okay, what I'm --

7 CHAIRMAN GOLDWAY: And I mean one assumes
8 that the competitive prices will come out at the same
9 time that they came out last year, which is January.

10 THE WITNESS: Yes, we intend to file --

11 CHAIRMAN GOLDWAY: So if the Commission
12 gives you the approval to raise these prices --

13 THE WITNESS: Yes.

14 CHAIRMAN GOLDWAY: You have the discretion
15 to raise prices for priority mail anyway.

16 THE WITNESS: Yes, yes.

17 CHAIRMAN GOLDWAY: One assumes that those
18 prices will be higher than these prices?

19 THE WITNESS: All I, I have been informed
20 that the people who price the competitive products
21 will not price priority mail below that. I will
22 convey your concerns to them about that, that you
23 believe they should be higher.

24 CHAIRMAN GOLDWAY: You could also tell them
25 that, you know, the PAEA really anticipated that there

1 was going to be a lot more profit generated from those
2 competitive products than we've seen so far, and I'm
3 not sure keeping prices below or at parcel post prices
4 is a good way to generate profit.

5 THE WITNESS: I will pass your concerns
6 along.

7 CHAIRMAN GOLDWAY: Commissioner Hammond,
8 Vice Chairman Hammond had a question about first class
9 mail, and I'm afraid since we were hungry and breaking
10 for lunch I didn't give him a chance to ask that
11 question.

12 THE WITNESS: Okay.

13 CHAIRMAN GOLDWAY: So I'm giving him that
14 opportunity now.

15 VICE CHAIRMAN HAMMOND: Thank you, Madam
16 Chairman. I know, Dr. Kiefer, we beat standard class
17 to death and beat periodicals flats to death, but we
18 haven't had the opportunity on first class presort
19 flats necessarily.

20 THE WITNESS: Okay.

21 VICE CHAIRMAN HAMMOND: So that's what I
22 wanted to get into because I had a special concern
23 about that. So in response to a couple of the
24 presiding officer information questions you told us
25 that relative price increases for flats in first class

1 standard and periodicals are basically based on
2 knowledge of the industries that use those products,
3 and I was wondering could you tell us what industries
4 are the major users of first class presort flats?

5 THE WITNESS: I have some ideas, but I think
6 I can give you a more precise list, I know that, well
7 I could --

8 VICE CHAIRMAN HAMMOND: Would you, if I were
9 to say --

10 THE WITNESS: Yes.

11 VICE CHAIRMAN HAMMOND: That financial
12 statements, insurance, shareholder reports, proxies,
13 et cetera, things like that, would you agree that
14 those could be the major users of presort first class
15 flats?

16 THE WITNESS: I know that they are
17 significant users. Their proportion of use is not
18 something that I can say with confidence without
19 checking.

20 VICE CHAIRMAN HAMMOND: But if we were
21 speaking at least in generality, they are users --

22 THE WITNESS: Okay, I can accept that.

23 VICE CHAIRMAN HAMMOND: I won't hold you to
24 specific volume amounts necessarily.

25 THE WITNESS: Okay.

1 VICE CHAIRMAN HAMMOND: Okay, if we can
2 assume that, okay. And basically from those that I
3 mentioned and those that you know of are some of those
4 mailers using first class instead of standard because
5 they're legally obligated to do so?

6 THE WITNESS: To the extent that they are
7 statements and communications that contain individual
8 correspondence or communications, yes they would be
9 required to do so.

10 VICE CHAIRMAN HAMMOND: Okay, so they're
11 basically what I have thought of for years as like
12 captive mailers and really don't have much choice.
13 They are told that they will provide that information
14 to the person and it's either going to be by first
15 class mail or as we get to electronic diversion it's
16 going to be one or the other, but first class mail,
17 which it goes into presort first class flats, would be
18 a good portion of that, wouldn't you say?

19 THE WITNESS: Yes.

20 VICE CHAIRMAN HAMMOND: Yes, okay. So how
21 would you characterize the current state of those
22 industries that use those first class flats?

23 THE WITNESS: Well, certainly the banking
24 industry is at least certain segments of the banking
25 industry has had some difficult times, and some of the

1 other ones, the financial industry has certainly had
2 some difficult times.

3 VICE CHAIRMAN HAMMOND: Okay, so and but I
4 do take it from your pricing proposal, because let's
5 see, roughly standard flats are getting about 5
6 percent, periodicals are getting about 8 percent, and
7 these first class presort flats are going to get about
8 a 12 percent increase, right?

9 THE WITNESS: They will get a, I believe
10 it's, yeah, 11 plus percent.

11 VICE CHAIRMAN HAMMOND: Okay, and they are
12 already well beyond their cost coverage for Postal
13 Service, are they not? If I were to say that they are
14 currently covered at least probably 130 percent if not
15 more, cost coverage currently, you probably would not
16 dispute that?

17 THE WITNESS: I don't have that number here.
18 I can't dispute it, I don't have the number.

19 VICE CHAIRMAN HAMMOND: Do you think they're
20 currently not covering their costs?

21 THE WITNESS: I don't have -- no, I don't
22 believe that they're not covering their costs, but I
23 don't have -- well, let me see. Okay, I look at Mr.
24 Masse's paper, I think first class flats have a
25 healthy cost coverage.

1 VICE CHAIRMAN HAMMOND: Okay, so those first
2 class presort flats are already more than covering
3 their costs, and they are for the most part people who
4 must be in the mail unless they receive specific
5 permission from people to be sent that information
6 electronically rather than being in the mail, and
7 they're going to receive at least, about a 12 percent
8 increase in this exigency case. And I take it from
9 the proposal that you think these industries that's in
10 these first class flats are in a better position to
11 withstand a large price increase than others, was that
12 your reasoning?

13 THE WITNESS: Well, in this particular case
14 I believe that, I've discussed this in my statement,
15 that much of this increase is coming about because of
16 the, the Postal Service is trying to respond to
17 directives, the problem is that some of the, much of
18 this mail is presort as you say, it's workshared,
19 heavily workshared, and these pieces, the Commission's
20 rules and the PAEA require us to set the presort
21 discounts at no more than avoided costs or otherwise
22 provide a justification, one of the four allowable
23 justifications.

24 As I explained in the statement there was an
25 error discovered in the flats cost model in 2008 that

1 lead us to realize that the avoided costs were much
2 lower than we had thought previously, and so that
3 therefore the discounts were too high, that the
4 passthroughs were substantially over 100 percent. And
5 so the Postal Service has been taking steps, and I
6 believe the Commission has been sort of working with
7 us on this and the fact that we didn't try to reduce
8 the passthroughs down to 100 percent all in one big
9 step but we're taking significant steps along the way,
10 and we were giving them various categories of above
11 average increases in order to reduce the passthroughs.

12 Now even with the fairly high increases that
13 we are proposing for standard mail presort flats in
14 this particular price adjustment, we are still going
15 to be above 100 percent cost coverage. We don't think
16 that we can go, we didn't think we could go any
17 farther, and I believe that we used the rate shock
18 justification for sort of as a reason to limit these
19 to 100 percent. But we felt --

20 VICE CHAIRMAN HAMMOND: So you're saying,
21 you just said "rate shock". Does that mean you would
22 have really liked to have raised them higher than the
23 12 percent that you're proposing now?

24 THE WITNESS: No, no, as I said we were
25 responding to the Commission's directives to reduce

1 excess passthroughs to 100 percent but we were using
2 rate shock as the justification for not going higher.
3 I mean again this is a balancing situation between
4 trying to work to adjust the passthroughs to where the
5 Commission would like to have them and concern over
6 the amount of increase that and its impact would have.
7 So at this particular time we felt that we should not
8 be asking these mailers to go above, I think it was 11
9 to 12 percent.

10 CHAIRMAN GOLDWAY: And by the 12 percent
11 increase what is the passthrough percentage that
12 remains?

13 THE WITNESS: At the top of the presort
14 ladder, the automation ADC flats passthrough relative
15 to the automation mixed ADC flats after this price
16 changes will be 220 percent, which is still --

17 CHAIRMAN GOLDWAY: 400?

18 THE WITNESS: I'm sorry --

19 CHAIRMAN GOLDWAY: 200.

20 THE WITNESS: 220 percent. So, which is
21 significantly above the 100 percent direction we're
22 heading in.

23 VICE CHAIRMAN HAMMOND: So it is the fault
24 of the Postal Regulatory Commission and the postal
25 reform legislation that you proposed a 12 percent

1 price increase here?

2 THE WITNESS: Well --

3 VICE CHAIRMAN HAMMOND: I'm sorry, that's
4 what I thought I heard you say. Is that correct?

5 THE WITNESS: I was not saying it was
6 anybody's fault, I was saying we were trying to
7 respond to the requirements in the law and in the
8 Commission's rules to adjust these down to 100
9 percent, and we gave an above average increase up to
10 the point where we felt that the rate shock
11 justification would apply.

12 VICE CHAIRMAN HAMMOND: Well, I am not sure
13 I agree, but --

14 THE WITNESS: I understand.

15 VICE CHAIRMAN HAMMOND: But I won't go much
16 --

17 CHAIRMAN GOLDWAY: Can I ask? I don't
18 recall whether the extra ounce rate affects this
19 product at all. Did you say -- not giving an increase
20 on the extra ounce rate to this product or are you?
21 Does that make a difference in what the averages will
22 be?

23 THE WITNESS: I'll have to look that up.
24 Let's see.

25 CHAIRMAN GOLDWAY: Am I right in that? I

1 think the increase is large but when you take into
2 account that they're not getting the increase in the
3 extra ounce it winds up being less, or am I wrong?
4 I'm wrong about that?

5 THE WITNESS: For presorted flats the
6 additional ounce rate does increase from 17 cents to
7 18 cents.

8 CHAIRMAN GOLDWAY: Oh it does.

9 THE WITNESS: But that particular increase,
10 what 18 over 17 is, I don't know I'm going to say it's
11 maybe 5 or 6 percent, so it's, you know, it's a penny
12 but it's about 5 or 6 percent, so it would have the
13 effect of for heavier pieces it would have the effect
14 of drawing down the --

15 CHAIRMAN GOLDWAY: I think that's what our
16 staff said that the average weight of those --

17 THE WITNESS: Yeah, they tend to be higher.

18 CHAIRMAN GOLDWAY: Annual reports and
19 various documents that we get in the mail, financial
20 documents, is on the heavier side.

21 VICE CHAIRMAN HAMMOND: Well, I mean I don't
22 know, I'm --

23 CHAIRMAN GOLDWAY: So that the average
24 increase is not quite as high, but it's still higher
25 than the rest of the class.

1 VICE CHAIRMAN HAMMOND: Yes, we're still
2 coming up with the 12 percent increase and I'm told
3 that we achieve a 220 percent passthrough with a 5
4 percent increase. That sound make any sense?

5 CHAIRMAN GOLDWAY: No, I don't --

6 THE WITNESS: No, no, the 220 percent was
7 the passthrough between the benchmark for ADC
8 automation flats, which is the, it's the first level
9 of presort, and its benchmark which is the mixed ADC
10 flats, it's 220 percent after the 12 percent. In
11 other words had the increase been lower the
12 passthrough would have been higher than 220 percent,
13 and conversely had the increase in the price been
14 higher the passthrough would have been lower.

15 VICE CHAIRMAN HAMMOND: Well, do you see any
16 potential for the Postal Service to assist in its own
17 demise by driving mail to electronic delivery by such
18 price increases? I mean that just, you know, those
19 people have to mail or they have to get permission
20 from someone, millions of people, to deliver
21 electronically. Now, you know, we've all been getting
22 for years now the request that we do the simple
23 electronic delivery and a bunch of us have not done
24 so, but wouldn't, couldn't this be the increase which
25 gets those companies, those institutions, those

1 businesses, to think, well this is going to be worth
2 it for us to actually spend money now to get people to
3 go to electronic delivery which will save us in the
4 long run because we can leave the U.S. Postal Service?

5 THE WITNESS: I understand your concerns,
6 and I think that we have in general made the argument
7 in respect to other categories of mail that, the exact
8 same argument you made. I take it from your statement
9 that you think we've gone too far on this one.

10 VICE CHAIRMAN HAMMOND: Yes, I'm sorry, I
11 do.

12 THE WITNESS: I understand.

13 VICE CHAIRMAN HAMMOND: So I will not pursue
14 this any further. Thank you very much.

15 CHAIRMAN GOLDWAY: I'm glad you brought that
16 up, Commissioner Hammond, we'll certainly discuss it
17 among ourselves as well, thank you. So we have one
18 more category which is special services. And I had
19 better get out, I got so involved in the first class I
20 forgot about this. So this is a question about
21 confirm service.

22 THE WITNESS: Okay.

23 CHAIRMAN GOLDWAY: Which had a negative
24 contribution in Fiscal Year 2009. On page 52 you
25 stated that a primary cost driver for confirm is data

1 storage that has largely been driven by the scans
2 provided to platinum service tier customers. Further
3 you stated that you believe that the increases given
4 to each of the four tiers will be sufficient to
5 achieve full cost coverage for confirm. How did you
6 determine the price increase for each tier?

7 THE WITNESS: I believe that the, let me see
8 if I have. When we change the prices of the various
9 tiers in confirm the subscription prices for the
10 bronze, silver, and gold categories, that is the
11 smaller user type categories, we attempted to put
12 those within the general increase range of 4 to 6
13 percent, and the fees for confirm range from 4 percent
14 for bronze and silver, 4 percent increases for bronze
15 and silver, and 6 percent for gold.

16 Then because, as stated or as mentioned in
17 the statement, we believe that the costs have been
18 driven largely by the extra data storage needed to
19 handle the demands of the platinum customers, we
20 determined what would be the amount of increase needed
21 to reach a full cost coverage for the product, and
22 that was the increase that was given to the, assigned
23 to the platinum customers.

24 CHAIRMAN GOLDWAY: So the 25.6 percent
25 increase is what you determined was necessary to cover

1 the cost?

2 THE WITNESS: Well, the data, that may be --
3 yes, if that's the, the data I have here is by tier,
4 but if the 25.6 is the increase for all of confirm,
5 yes, that would be --

6 CHAIRMAN GOLDWAY: No, no, that's just for
7 platinum.

8 THE WITNESS: Oh, platinum? I have a
9 different number here. It actually says 28 percent.

10 CHAIRMAN GOLDWAY: You have 28? We have, my
11 chart says 25.6 percent.

12 THE WITNESS: Oh, okay, well.

13 CHAIRMAN GOLDWAY: But how did you get that
14 number? You know, did you look at the cost of data
15 storage?

16 THE WITNESS: Well, it was, we looked at the
17 cost of the product, of confirm. I mean didn't break
18 out specifically.

19 CHAIRMAN GOLDWAY: So you just looked at the
20 gap between the overall cost of the service and what
21 was lost in 2009?

22 THE WITNESS: Right, right.

23 CHAIRMAN GOLDWAY: Gave the others a sort of
24 general increase and put the biggest amount on
25 platinum assuming that they're the ones who use the

1 most of it and --

2 THE WITNESS: They're the ones who, it was
3 our belief, yes, that they were the ones who are
4 driving the cost and resulting in the fact that we
5 were failing to cover our costs, and so --

6 CHAIRMAN GOLDWAY: So and in 2009 in the ACD
7 you explained that the big cost increase was because
8 you had to purchase a whole lot of new data storage
9 processing equipment to handle confirm, and that's why
10 the prices went up?

11 THE WITNESS: Yeah, well the platinum users
12 have unlimited scans, and so these are largely
13 resellers, they're ones who buy this service and then
14 sell it to others. And, you know, the more they, if
15 it is underpriced they will sell, they will put ever
16 increasing demands on us and we have to go out and buy
17 additional storage. So it was our belief that these
18 customers were primarily responsible for the gap and
19 so we gave the others a price changes that fell within
20 the prescribed range and asked the platinum
21 subscribers to cover the difference.

22 CHAIRMAN GOLDWAY: So my staff is concerned
23 that you don't yet know what your budget is for 2011,
24 and these prices would go into effect in 2011, and
25 that there might be significant additional

1 expenditures for new data storage. If you're just
2 pricing up to what was expended in 2009 do you have
3 any indication that these new prices are in fact going
4 to cover the costs of 2011?

5 THE WITNESS: I understand your concerns.
6 I'm looking at Mr. Masse's tables and I don't believe
7 that they have, I don't see confirm broken out.
8 Clearly if these -- I understand the concern but all I
9 can say at this time is that as we, if we increase the
10 price to the resellers some of that may be passed
11 along to some of their customers, which may have the
12 effect of dampening the sort of the growth in the
13 demand that the resellers place on us to buy new
14 storage, if you know what I'm saying. So in other
15 words they will have to increase the price and that
16 may sort of help to bring the demand down a little bit
17 so that the resellers are not going to be asking us
18 for more --

19 CHAIRMAN GOLDWAY: But we hate to see more
20 loss making products. So could you perhaps provide an
21 answer to my question about your planned expenditures
22 for IT and data collection with regard to confirm
23 service in 2011?

24 THE WITNESS: Okay, yes, I'll pass this
25 along so we can get that for you to the extent that --

1 MR. RUBIN: We'll be happy to. We tried to
2 respond to this in providing information in request
3 number 3 question 15, and we weren't, I guess, yeah,
4 it says Postal Service has not fully determined plans
5 for Fiscal Year 2011.

6 CHAIRMAN GOLDWAY: Yes, so --

7 MR. RUBIN: So do we --

8 CHAIRMAN GOLDWAY: You may not have fully
9 determined them, but I'm sure you have as we do some
10 general indications whether that's going to be a
11 potential area for spending.

12 THE WITNESS: Okay.

13 CHAIRMAN GOLDWAY: And we would like to know
14 what you know.

15 THE WITNESS: Well, we will make sure that
16 we provide the best information we have on that.

17 CHAIRMAN GOLDWAY: Okay.

18 MR. RUBIN: Okay.

19 CHAIRMAN GOLDWAY: Thank you. That
20 concludes my list of questions. Commissioner Langley?

21 COMMISSIONER LANGLEY: I have just a
22 question.

23 THE WITNESS: Sure.

24 COMMISSIONER LANGLEY: You've been very
25 straightforward, forthright, answering when you can.

1 If the exigent rate increase isn't approved has Postal
2 management asked you to prepare for any contingency?

3 THE WITNESS: No.

4 COMMISSIONER LANGLEY: Thank you.

5 CHAIRMAN GOLDWAY: In other words you
6 haven't looked at the legal rate cap to see what you
7 could do with that?

8 THE WITNESS: We have not prepared any
9 prices that are, that would fit into the price cap as
10 of I don't know what date. We are not a large staff,
11 and that is certainly a, would be a challenge to try
12 to pursue two sort of rate designs at the same time.
13 We haven't been asked to do that, no.

14 COMMISSIONER ACTON: Have you been asked to
15 perhaps estimate the approximate revenue that may be
16 available to the Service under the 1 percent cap?

17 COMMISSIONER LANGLEY: As well as the banked
18 amount.

19 THE WITNESS: Well, I should point out that
20 our pricing function, in the past we used to estimate
21 the revenue that, we don't do that anymore. I'm not
22 aware of whether our forecasting people or our budget
23 people were asked that question. We don't do revenue
24 projections anymore.

25 COMMISSIONER ACTON: Thank you.

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1 CHAIRMAN GOLDWAY: Any other questions?

2 (No response.)

3 CHAIRMAN GOLDWAY: Well, Dr. Kiefer, you
4 have done yeoman's duty today. We all appreciate your
5 answers and your patience with us, and as I said
6 yesterday I think we all have the best interests of
7 the Postal Service at heart.

8 THE WITNESS: Absolutely.

9 CHAIRMAN GOLDWAY: But the questions in
10 front of us and in difficult times are not easy to
11 answer. And I hope that the concerns and questions
12 raised by the Commissioners here today will be brought
13 back to top level management in addition to the people
14 that you work with directly so that we can all come up
15 with better answers in the future. I would like to be
16 able to clarify just when we will get the answers to
17 questions that we've asked for in the last three days
18 from the Postal Service. Mr. Rubin, can you help me
19 with that?

20 MR. RUBIN: Our plan is to get them within a
21 week of each day's hearing.

22 CHAIRMAN GOLDWAY: Is that going to be
23 satisfactory, Mr. Sharfman, given how difficult it is
24 for us to answer questions?

25 MR. RUBIN: Well, also I expect to have

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1 POIRs to work on.

2 CHAIRMAN GOLDWAY: We're going to be
3 submitting additional POIRs, that's true.

4 MR. RUBIN: So, yeah.

5 THE WITNESS: We are a lean staff.

6 CHAIRMAN GOLDWAY: All right, we will agree
7 then that within a week, seven days including
8 Saturdays and Sundays, we will receive answers to the
9 questions that we asked from the bench for each day
10 that we asked them.

11 MR. RUBIN: Yes.

12 CHAIRMAN GOLDWAY: Thank you.

13 VICE CHAIRMAN HAMMOND: Madam Chairman?

14 CHAIRMAN GOLDWAY: Commissioner Hammond?

15 VICE CHAIRMAN HAMMOND: While you're on
16 that, I noted you made comment this morning of this
17 suggestion of request information by the Alliance of
18 Nonprofit Mailers and Magazine Publishers which you
19 said we're going to honor, and I'm certainly glad that
20 you're seeing that this is done. They put a request
21 that that information be provided by Friday, August
22 13th.

23 CHAIRMAN GOLDWAY: Is that possible? Yes.

24 VICE CHAIRMAN HAMMOND: So because that is
25 possible, we're not talking about what you were doing

1 today being a whole week away from before they would
2 provide that or, because I know we all care about this
3 was a very excellent suggestion for request for
4 information.

5 CHAIRMAN GOLDWAY: Yes.

6 MR. RUBIN: Well, I had in mind that we had
7 that deadline for tomorrow.

8 CHAIRMAN GOLDWAY: Okay, that deadline is
9 for tomorrow, but the questions that we asked from the
10 bench are a week from when we asked them.

11 MR. RUBIN: Yes.

12 CHAIRMAN GOLDWAY: Okay, and we will submit
13 POIRs and if we need them to be answered sooner than
14 that we'll have to indicate that to you, we'll see
15 what the schedule is. After all we have a very
16 limited time to make a decision. With that, I will
17 adjourn these hearings, conclude them, and again thank
18 you, Dr. Kiefer, thanks to the Postal Service
19 attorneys for their participation and for the
20 audience. And we'll get back to work behind closed
21 doors to try and sort out these issues. Thank you
22 very much.

23 (Whereupon, at 4:20 p.m., the hearing in the
24 above-entitled matter was adjourned and concluded.)

25 //

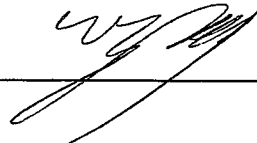
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CASE TITLE: Rate Adjustment Due to Extraordinary
HEARING DATE: 8/12/10
LOCATION:

WDC

I hereby certify that the proceedings and evidence are contained fully and accurately on the tapes and notes or digital recording reported by me at the hearing in the above case before the PRC,

Date: 8/12/10



Official Reporter
Heritage Reporting Corporation
Suite 600
1220 L Street, N.W.
Washington, D.C. 20005-4018